

(1992) 10 DEL CK 0017

In the Delhi High Court

Case No : Income Tax R. No. 65 of 1982

Commissioner of Income Tax

APPELLANT

Vs

Modi Industries Ltd.

RESPONDENT

Date of Decision : 12-10-1992

Acts Referred:

Citation : (1993) 200 ITR 341 : (1993) 68 TAXMAN 114

Hon'ble Judges : P.K. Bahri, J;B.N. Kirpal, J

Bench : Division Bench

Advocate : Rajendra and D.C. Taneja, S.K. Aggarwal, for the Appellant;

Judgement

B.N. Kirpal, J.—Two questions of law have been referred to this court by the Income Tax (Tribunal) u/s 256(1) of the Act, one question has been referred at the instance of the Revenue and the other at the instance of the assessed.

2. The question which has been referred at the instance of the assessed is as follows :

"Whether there was any evidence before the Tribunal to arrive at the finding that the applicant had not proved that the expenditure of Rs. 1,42,289 representing a part of the commission paid to M/s. Standard Electrode Corporation was an expenditure incurred wholly and exclusively for the purposes of business ?"

3. This reference is in respect of the assessment year 1965-66. Some commission had been paid by the assessed to M/s. Standard Electrode Corporation. Out of the total amount so paid, a sum of Rs. 1,42,289 was disallowed. This Corporation had been appointed as the sole selling agent of the assessed-company for a period of five years with effect from July 27, 1963, vide resolution of the board of directors of the assessed-company dated July 27, 1963. The Income Tax Officer came to the conclusion that the expense to the extent of Rs. 1,42,289 was not legally warranted and the same was disallowed.

4. The Appellate Assistant Commissioner, in appeal, came to the conclusion that

there was no evidence to show that M/s. Standard Electrode Corporation rendered any service for which they could be paid commission on the ground of commercial expediency. This conclusion of the Appellate Assistant Commissioner was in consonance with the earlier decision for the assessment year 1964-65.

5. In further appeal to the Income Tax Tribunal, the disallowance was upheld. The Tribunal also followed a similar view which had been taken by it in the assessed's case in respect of an earlier assessment year 1964-65. As the reference had been made in respect of the assessment year 1964-65, for the present year in question, viz., 1965-66, the aforesaid question of law was again referred by the Tribunal, at the instance of the assessed.

6. In respect of the assessment year 1964-65, a similar question of law was answered against the assessed by this court in ITR No. 64 of 1982 (Modi Industries Ltd. Vs. Commissioner of Income Tax, , vide judgment dated August 6, 1992. The effect of this was that the disallowance of the commission paid to M/s. Standard Electrode Corporation was upheld. Following the said decision the only conclusion which we can arrive at is that there was evidence before the Tribunal on which it could legitimately come to the conclusion that the sum of Rs. 1,42,289 should be disallowed. The aforesaid question is, Therefore, answered in favor of the Revenue and against the assessed.

7. The question which has been referred at the instance of the Revenue is as follows :

"Whether, on the facts and in the circumstances of the case, the Tribunal was justified in holding that the business of manufacture of M. S. special alloy wires and billets was an extension of business and not a new business and allowing a deduction of the sum of Rs. 2,61,918 on account of expenditure incurred for raising of the loans by the issue of debentures ?"

8. Briefly stated the facts are that the assessed had claimed an expenditure of Rs. 3,12,704 consisting of underwriting commission, brokerage, cost of stamp paper, registration charges, advertisements and expenses on the issue of prospectus. Out of this a sum of Rs. 2,61,918 was claimed as business expenditure. The Income Tax officer found that the said expenditure included a provision of Rs. 50,786 made for registration expenses of the debentures trust deed which was to be got registered in the following year. He, Therefore, considered the claim of Rs. 2,61,918, out of the total claim of Rs. 3,12,704, on merits. This claim was disallowed by the Income Tax Officer who held that debentures in this case were specially issued for raising funds for being used in setting up a new steel unit which did not start working during this year and in setting up this unit the assessed had engaged itself in an activity which was not akin or related to its usual business.

9. The assessed thereafter filed an appeal before the Appellate Assistant Commissioner and contended that the business of manufacture of alloy steel billets, which was sought to be undertaken, was not a new one but was an

extension of the existing business. It was submitted that the debenture amount received formed part of the aggregate sums of the company and they were so inextricably mixed up that the amount received by way of issue of debentures could not be separately identified.

10. The Appellate Assistant Commissioner, however, came to the conclusion that the business of manufacture of alloy steel and billets was a new business and he came to this conclusion for the following reasons :

"(i) The nature of the items to be manufactured was not in any way connected with the items already manufactured by the assessed-company and with a view to finance the scheme, the Controller of Capital Issues was approached for the issue of 7 per cent. debentures of the face value of Rs. 60 lakhs out of which Rs. 50 lakhs were actually issued.

(ii) Separate books of account were maintained for this unit which had a separate staff to manage and control its day to day activities.

(iii) A separate factory building was constructed adjoining the other units in which the steel unit was erected.

(iv) The financial management was also separate from the other units because the amount loaned from the head office was separately shown in the balance-sheet and separate profits were worked out for this unit on the basis of its financial sets of account. Till the unit started production a separate account was maintained in the central office set of books."

11. A further appeal was filed by the assessed to the Tribunal. The Tribunal referred to the decision of the Supreme Court in the case of Commissioner of Income Tax, Madras Vs. Prithvi Insurance Co. Ltd., , wherein the Supreme Court had followed the observations of Rowlatt J. in the case of Scales v. George Thompson and Co. Ltd. [1927] 13 TC 83, where the test for determining whether it was the same business or not had been enunciated. This test was whether there was any interconnection, any interlacing, any interdependence, any unity at all embracing those two businesses ? The test laid down by Rowlatt J. was kept in view by the Tribunal and it came to the conclusion that "on facts we have found that the management of the new business and the earlier business was the same and there was unity of control and a common fund."

12. The claim of the assessed was accordingly allowed by the Tribunal. It is thereafter that the Commissioner of Income Tax filed an application and the aforesaid question of law has been referred to this court.

13. In order to decide the question so referred it is necessary to deal with various decisions which have been cited at the Bar.

14. In Commissioner of Income Tax, Madras Vs. Prithvi Insurance Co. Ltd., the assessed was carrying on the business of life insurance as well as general insurance. A question arose whether the unabsorbed losses of one type of

business (life insurance) could be set off against the profits of the general insurance business. After referring to the aforesaid observation of Rowlatt J. the Supreme Court came to the conclusion, in that case (at page 638) :

"That interconnection, interlacing, interdependence and unity are furnished in this case by the existence of common management, common business organisation, common administration, common fund and a common place of business."

15. In *Hooghly Trust (Private) Ltd. Vs. Commissioner of Income Tax, West Bengal and Andaman and Nicobar Islands*, , a similar question again arose. The assessed in that case acted as a distributing agent of the Government for cloth and cement. The cloth business had been started in 1946 and the same was brought under Governmental control thereafter. The assessed had also been doing business in several other commodities and the question arose whether different commodities in which the business was being done could be regarded as the same business or different businesses. The Tribunal decided in favor of the assessed but the High Court came to a different conclusion and it held that the inference drawn by the Appellate Tribunal was not warranted by the facts on record and that the cloth business was separate from the appellant's business in the general section notwithstanding that there was some interconnection of expenses or control. The assessed thereafter filed an appeal to the Supreme Court and the Supreme Court came to the conclusion that in the absence of a proper question about the validity of the findings of facts arrived at by the Tribunal, it was not open to the High Court to accept the findings of the Appellate Assistant Commissioner or to come to any independent conclusion itself on facts. The Supreme Court further reaffirmed the principle enunciated in *Commissioner of Income Tax, Madras Vs. Prithvi Insurance Co. Ltd.*, and came to the conclusion that if there was common management, common business organisation, common administration, common fund and common place of business then, one could come to the conclusion that there was interconnection, interlacing and interdependence which would mean that it was the same business. In *Produce Exchange Corporation Ltd. Vs. Commissioner of Income Tax (Central), Calcutta*, , the appellant-company carried on business as a dealer in diverse commodities and also in stocks and shares. It suffered losses in the sale of shares and it claimed to carry forward and set off the same against the profits of subsequent years from transactions in other commodities. While the Tribunal had found that there was complete unity of control and shares were one out of a number of commodities in which the company dealt in the ordinary course of business and that there was no element of diversity or distinction or separateness about the transaction in shares, and, accordingly, upheld the claim, the High Court, on the other hand, on a reference, held that the essential matter to be considered was the nature of the two lines of business and not merely their unity of control and, Therefore, the Tribunal, according to the High Court, had erred in holding that the whole trading activity formed one business. The Supreme Court, on appeal, reversed the decision of the High Court and came to the conclusion that the

decisive test was unity of control and not the nature of the two lines of business. It further came to the conclusion that the Tribunal was right in holding that the share business and other businesses carried on by the appellant-company constituted the same business within the meaning of section 24(2) of the Indian Income Tax Act, 1922. In arriving at this conclusion the Supreme Court referred to the aforesaid observations of Rowlatt J. in Scales' case [1927] 13 TC 83 and also to the principles laid down by the Supreme Court itself in Commissioner of Income Tax, Madras Vs. Prithvi Insurance Co. Ltd., .

16. To similar effect is another decision of the Supreme Court in the case of B.R. Limited Vs. V.P. Gupta, Commissioner of Income Tax, Bombay, . In that case the appellant-company had incurred a loss in the business of import and sale of fabrics in the calendar year 1952. It closed down that business and in the following year it started the business of exporting cotton textiles and earned profits therein. A question arose whether it was the same business or not for the purpose of setting off of carried forward loss. The Supreme Court following its decisions in Produce Exchange Corporation Ltd. Vs. Commissioner of Income Tax (Central), Calcutta, and Commissioner of Income Tax, Madras Vs. Prithvi Insurance Co. Ltd., came to the conclusion that (at page 654) :

"Thus, the unity of control and the other circumstances adverted to above show that there was dovetailing or interlacing between the business of import and the business of export carried on by the assessed and that they constitute the same business."

17. In coming to this conclusion, the Supreme Court, while referring to the case of Produce Exchange Corporation Ltd. Vs. Commissioner of Income Tax (Central), Calcutta, , observed that the decisive test was the unity of control and not the nature of the two lines of business.

18. From the aforesaid observations of the Supreme Court in the case of Commissioner of Income Tax, Madras Vs. Prithvi Insurance Co. Ltd., , Produce Exchange Corporation Ltd. Vs. Commissioner of Income Tax (Central), Calcutta, and B.R. Limited Vs. V.P. Gupta, Commissioner of Income Tax, Bombay, , it would clearly follow that the nature of the lines of business is not relevant but what is of importance is the unity of control and interlacing of the two businesses.

19. In The Standard Refinery and Distillery Ltd. Vs. Commissioner of Income Tax, Calcutta, , the assessed-company owned a distillery and had acquired a sugar refinery. During the period in question the assessed also purchased and sold shares of a sugar and gur refining company and had suffered a loss therein. The question which arose for consideration before the Supreme Court was whether the loss so suffered in the sale of shares could be carried forward and set off against the income from sugar manufacturing and distillery. The Tribunal had found that there was a single trading and profit and loss account of the business. The share transaction as well as the business had been dealt with by a common organisation, the business of the company as well as the transaction in shares

were attended to as a part and parcel of the business of the company and a common fund was utilised both for business purposes as well as for the purpose of purchase of shares. It was in view of this finding of fact that the Supreme Court observed that the concepts of interconnection and interlacing, interdependence and unity were not free from ambiguity. It then referred to the decision in the cases of *The Standard Refinery and Distillery Ltd. Vs. Commissioner of Income Tax, Calcutta*, and *Produce Exchange Corporation Ltd. Vs. Commissioner of Income Tax (Central), Calcutta*, and held that the Supreme Court had ruled that the decisive test was unity of control and not the nature of the two lines of business". Following its earlier decisions, the Supreme Court in the case of *The Standard Refinery and Distillery Ltd. Vs. Commissioner of Income Tax, Calcutta*, came to the conclusion that the assessed was entitled to set off losses in the sale of shares against the income from sugar manufacturing and distillery. The principle on which this decision was based was that there was unity of control between the two types of business.

20. Learned counsel for the Commissioner, however, has strongly relied upon a decision of the Supreme Court in the case of *L.M. Chhabda and Sons Vs. Commissioner of Income Tax, Gujarat*, . At the outset we would like to point out that the Supreme Court in *L.M. Chhabda and Sons Vs. Commissioner of Income Tax, Gujarat*, did not consider or refer to its earlier decision in *Commissioner of Income Tax, Madras Vs. Prithvi Insurance Co. Ltd.*, and, surprisingly, *L.M. Chhabda and Sons Vs. Commissioner of Income Tax, Gujarat*, is not referred to by the Supreme Court in its four subsequent decisions in the cases of *Produce Exchange Corporation Ltd. Vs. Commissioner of Income Tax (Central), Calcutta*, , *B.R. Limited Vs. V.P. Gupta, Commissioner of Income Tax, Bombay*, , *Hooghly Trust (Private) Ltd. Vs. Commissioner of Income Tax, West Bengal and Andaman and Nicobar Islands*, and *The Standard Refinery and Distillery Ltd. Vs. Commissioner of Income Tax, Calcutta*, . Perhaps the reason for the case of *L.M. Chhabda and Sons Vs. Commissioner of Income Tax, Gujarat*, , not being referred to was that the supreme Court held in that case that (at page 642) :

"It was for the appellants to establish that different ventures constitute parts of the same business. There is in this case no evidence about unity of control and management, or interrelation of the business, or employment of the same staff to run the business, or the possibility of one theatre being closed without affecting the rest of the business."

21. In the present case, however, the finding of fact arrived at by the Tribunal, on the basis of evidence on record, is that the management of the new business and the earlier business was the same and there was also unity of control and a common fund. Shri Rajendra submits that this finding is without any basis. But the Department has not challenged the correctness of this finding. The assessed, as noted by the Income Tax Officer, is engaged in the manufacture of various commodities like sugar, vanaspati, soaps, paints and varnish, torch, lantern, etc. All that the assessed did now was to start manufacturing a new commodity. In a

larger sense the business of the assessed remained the same, viz., the business of manufacture. It was already manufacturing diverse items and a new item was added to this business. The facts found by the Tribunal are that there was complete unity of control and there was a common fund and these factors have been regarded as most material by the Supreme Court as is evident from the case of *The Standard Refinery and Distillery Ltd. Vs. Commissioner of Income Tax, Calcutta*, and the other cases referred to therein.

22. In view of the above the only conclusion which can be arrived at, Therefore, is that the Tribunal was justified in holding that the business of manufacture of special alloy wires and billets was an extension of the business and not a new business. The question referred is, Therefore, answered in the affirmative and in favor of the assessed.

23. There will be no order as to costs.