

(1985) 07 PAT CK 0021

In the Patna High Court

Case No : Taxation Case No's. 68 to 70 of 1973

Sardar Prit Inder Singh

APPELLANT

Vs

Commissioner of Income Tax

RESPONDENT

Date of Decision : 23-07-1985

Acts Referred:

Income Tax Act, 1922 — Section 10(1)
Income Tax Act, 1961 — Section 256(1)

Citation : (1986) 50 CTR 185 : (1986) 160 ITR 493 : (1986) 27 TAXMAN 524

Hon'ble Judges : Uday Sinha, J; Nazir Ahmad, J

Bench : Division Bench

Advocate : Pawan Kumar, for the Appellant; Shambhu Sharan, for the Respondent

Judgement

Nazir Ahmad, J.—A consolidated statement of the case has been submitted by the Income Tax Appellate Tribunal, Patna Bench, Patna (hereinafter referred to as "the Tribunal"), u/s 256(1) of the Income Tax Act, 1961 (hereinafter referred to as "the Act"), referring the following common question of law for the assessment years 1968-69, 1969-70 and 1970-71 :

" Whether, on the facts and in the circumstances of the case, the Tribunal was correct in holding that sums of Rs. 13,375, Rs. 12,314 and Rs. 1,594 in the assessment years 1968-69, 1969-70 and 1970-71, respectively, were not allowable as deductions in computing the income of the assessee ? "

2. From the facts as found from the statement of the case as well as the order of the Tribunal, it is evident that the assessee, as individual, is working as a contractor for supplying vegetables, fruits, dressed meat and meat on hoof, etc., to the army authorities in Assam.

3. Certain recoveries were effected by the military authorities from the assessee for either delay in supplying materials or supplying materials of sub-standard quality. These recoveries were effected under the agreement. The recoveries

effected for the assessment years 1968-69, 1969-70 and 1970-71 were Rs. 13,375, Rs. 12,314 and Rs. 1,594, respectively.

4. The Income Tax Officer while assessing the assessee noted these recoveries in the assessment years 1968-69 and 1969-70, but in the assessment year 1970-71, the assessee could not get the voucher receipts for deductions from the value of materials. Under the circumstances, the Income Tax Officer estimated the net profit at 10 percent, on the net receipts after allowing the recoveries made by the contractor in the assessment years 1968-69 and 1969-70, but in the assessment year 1970-71 on the net receipt, he took the net profit on estimate at 10 per cent.

5. The assessee appealed before the Appellate Assistant Commissioner and the Appellate Assistant Commissioner estimated the net profit at 71 per cent. on the net receipt. However, the assessee also claimed before the Appellate Assistant Commissioner that the recoveries made for the delayed supplies of materials and for the supply of sub-standard materials to the army authorities should also be allowed as business expenditure as they were deducted from the bills by way of penalty or damages. The Appellate Assistant Commissioner allowed the amounts of recoveries from the bills of the assessee treating them as business expenditure.

6. On appeal to the Appellate Tribunal, it was submitted on behalf of the Department that these amounts were recovered from the assessee by the military authorities for either delay in making supplies or for supplying materials of sub-standard quality. It was further urged that in case there was a delay in the supply of the materials, the army authorities would purchase the same from the market and the difference between the contracted rate and the market rate would be recovered from the contractor. It was also submitted that the army authorities would have also recovered the difference between the market rate and the contracted rate in case sub-standard qualities of materials were supplied. It was further pointed out by the Department that there is no material before the Tribunal from which the Tribunal may conclude as to how much recoveries were effected for the delay in supplying the materials and how much recoveries were effected for supplying the sub-standard quality of materials. It was also urged that these recoveries were by way of damages for breach of the terms of agreement and the same could not be allowed as deduction. The Tribunal agreed with the submissions of the Department and it held that when there is an agreement existing between the parties, both the parties are supposed to conform to the conditions contained in the agreement and in case one of the parties commits breach of the terms of contract on the basis of which the other party recovers the damage, such damage could not be allowed as deduction. The Tribunal also held that there was no material before the Tribunal from which the Tribunal may conclude that the delay effected in supplying the materials was for no fault of the assessee nor was there any material before the Tribunal from which the Tribunal could conclude that the assessee supplied materials of

standard quality which was erroneously held to be of sub-standard quality by the military authorities and, in those circumstances, the Tribunal held that the amounts of Rs. 13,375, Rs. 12,314 and Rs. 1,594, respectively, for the three assessment years were not allowable deductions.

7. Mr. Shambhu Sharan for the Revenue has relied on the order of the Tribunal and has submitted that where there is an agreement existing between the parties, both the parties are supposed to conform to the conditions contained in the agreement and that in case one of the parties commits breach of the terms of the contract on the basis of which the other party recovers the damage, such damage could not be allowed as deduction. However, he has not been able to cite any authority to support his contention. I also find that the Tribunal has wrongly placed the onus on the assessee to prove that the delay effected in supplying the materials was for no fault of the assessee or to prove that the assessee supplied materials of standard quality which was erroneously held to be of sub-standard quality by the military authorities. Under the circumstances, the only fact which remains on record is that the military authorities made deductions from the bills of the assessee on account of delay in the supply of the materials or on account of supplying sub-standard quality of materials.

8. Mr. Pawan Kumar has relied on the case of Commissioner of Income Tax Vs. Prafulla Kumar Mallik, . In this case, it was held that it was an inevitable consequence of the assessee's business as a paddy procuring agent that as a result of the goods delivered not being of contracted quality, breach of warranty, with the risk of liability to pay damages, should at times be committed and payment of such damages as a result of the breach of warranty in the course of or as a consequence of earning profits and gains, was incidental to the carrying on of the assessee's business : it was an unavoidable loss arising as one of the consequences of carrying on such business and, in those circumstances, the sum of Rs. 25,700 paid by the assessee by way of penalty to the Government was held to be an admissible deduction in computing the profits u/s 10(1) of the Indian Income Tax Act, 1922.

9. Mr. Pawan Kumar, on behalf of the assessee, has also relied on the case of Commissioner of Income Tax Vs. J.K. Cotton Spinning and Weaving Mills Co., , where the Allahabad High Court has held that the payment was not made for infraction of law : it was on account of a contractual obligation imposed by the Government, and the breach was in the contemplation of the parties and amounted to a risk in the carrying on of the business and was a commercial loss. Similar view has been held in the case of Commissioner of Income Tax, Gujarat-III Vs. Tarun Commercial Mills Co. Ltd., .

10. In view of these decisions, it has to be held that the damages paid by the assessee to the military authorities in the three assessment years as mentioned above are allowable as business expenditure u/s 37(1) of the Act, In view of my discussions above, I hold that the Tribunal has not taken a correct view of law in disallowing the claim of the assessee relating to the recoveries from the bills in

the three assessment years in question.

11. I accordingly hold that the Tribunal was not correct in holding that the sums of Rs. 13,375, Rs. 12,314 and Rs. 1,594 in the assessment years 1968-69, 1969-70 and 1970-71, respectively, were not allowable as deductions in computing the income of the assessee. The common question referred for the three assessment years in question is accordingly answered in favour of the assessee and against the Revenue. In the peculiar circumstances of the case, parties will bear their own costs.

Uday Sinha, J.

12. I agree.