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**(1997) 03 BOM CK 0049**

**In the Bombay High Court**

**Case No :** Income-tax References No's. 41 of 1989 and 118 of 1990

Tractor Engineers Ltd.

APPELLANT

Vs

Commissioner of Income Tax

RESPONDENT

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**Date of Decision :** 31-03-1997

**Acts Referred:**

Income Tax Act, 1961 — Section 2(31), 2(32), 28, 40

**Citation :** (1997) 228 ITR 531 : (1998) 1 MhLj 537

**Hon'ble Judges :** Pratibha Upasani, J;B.P. Saraf, J

**Bench :** Division Bench

**Advocate :** Deokinandan, J.D. Mistry, instructed by M/s. Kanga and Co., K.M.L. Majele, for the Appellant; Dr. V. Balasubramanian and J.P. Deodhar, for the Respondent

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## Judgement

DR. B.P. Saraf, J.—These references have been made by the Income Tax Appellate Tribunal u/s 256(1) of the Income Tax Act, 1961, at the instance of the assessee. Income Tax Reference No. 41 of 1989 pertains to the assessment year 1981-82 and Income Tax Reference No. 118 of 1990, pertains to the assessment year 1982-83. In the first reference, the following question has been referred to this court for opinion :

"Whether, on the facts and in the circumstances of the case, the Tribunal was justified in holding that the provisions of section 40(c) of the Income Tax Act, 1961, are applicable in the case of the appellant-company in so far as it concerned the payment of Rs. 1,52,368 made by it to M/s Larsen and Toubro Ltd. for having rendered services through a committee of directors ?"

2. In Income Tax Reference No. 118 of 1990, the following question has been referred to this court for opinion :

"Whether, on the facts and in the circumstances of the case, the Tribunal was justified in holding that the provisions of section 40(c) of the Income Tax Act, 1961, are applicable in the case of the appellant-company in so far as it

concerned the payment of Rs. 2,05,527 made by it to Larsen and Toubro Ltd. for having rendered services through a committee of directors ?"

3. The material facts giving rise to these references in both the years are identical. The assessee is a company carrying on the business of manufacturing trailer track parts of the tractors. Larsen and Toubro Ltd. had substantial interest in the assessee-company. The board of directors of Larsen and Toubro Ltd. passed a resolution to the effect that three directors of the said company would serve as members of the committee of the directors of the assessee-company and that the remuneration payable to them (exclusive of sitting fees as members of the said committee) would be held by them in trust for the said company, i.e., Larsen and Toubro Ltd. A sum of Rs. 1,52,368 was paid by the assessee-company to Larsen and Toubro Ltd. in the assessment year 1981-82 and a sum of Rs. 2,05,527 in the assessment year 1982-83 for the services rendered by it to the assessee-company through its three directors. The Income Tax Officer applied the provisions of section 40(c) of the Income Tax Act, 1961 ("the Act"), to the above payments and disallowed the claim of the assessee to the extent it was in excess of the amount permissible under that section.

4. The order of the Income Tax Officer was confirmed by the Commissioner of Income Tax (Appeals). The assessee appealed to the Income Tax Appellate Tribunal ("the Tribunal"). Before the Tribunal, it was contended by the assessee that section 40(c) had no application to the facts of the instant case because the payments had been made by the assessee to Larsen and Toubro Ltd., which is a holding company of the assessee-company. The case of the assessee before the Tribunal was that section 40(c) was applicable only to payments made to individuals and not to a limited company. This contention of the assessee was rejected by the Tribunal. The Tribunal observed that section 40(c) was applicable to any expenditure which resulted directly or indirectly in the provisions of any remuneration or benefit or amenity to a director or a person who has a substantial interest in the company. The Tribunal held that the expression "a person who has a substantial interest in the company" having been defined in section 2(32) of the Act to mean a person who is the beneficial owner of shares, carrying not less than 20 per cent. of the voting power, and the expression "person" having been defined in section 2(31) to include a "company", for the purposes of section 40(c) of the Act, a person having substantial interest in the company would include a company also. In the instant case, Larsen and Toubro Ltd. being the holding company of the assessee, the Tribunal was of the opinion that Larsen and Toubro Ltd. was a person who had substantial interest in the company within the meaning of section 40(c) of the Act. Aggrieved by the above finding of the Tribunal, the assessee sought for reference of the questions set out above to this court. Hence, these references.

5. So far as the above controversy referred to in the questions referred to us is concerned, Mr. Mistry, learned counsel for the assessee, stated before us that he does not want to contest the above finding of the Tribunal.

6. Mr. Mistry, however, wanted to argue, as one of the facets of the controversy, that the commission paid to Larsen and Toubro Ltd. would not fall within the ambit of section 40(c) of the Act because the commission was worked out as a percentage of the profits of the company. Reliance was placed in support of this contention upon the decisions of the Supreme Court in *Commissioner of Income Tax, Bombay Vs. M/s. Indian Engineering and Commercial Corporation Pvt. Ltd.*, and *Bharat Beedi Works (Pvt.) Ltd. and another etc. Vs. Commissioner of Income Tax*, . In reply, Dr. Balasubramanian, learned counsel for the Revenue, submitted that the controversy sought to be raised was not a facet of the controversy arising out of the questions referred to this court. According to him, it was a new controversy now sought to be raised for the first time which was not even supported by any factual finding of the Tribunal. He also submitted that in any event, on the face of the uncontroverted facts of this case, the ratio of the above decisions of the Supreme Court has no application to this case. According to Dr. Balasubramanian, this is not a case where the payments were made by the assessee-company to Larsen and Toubro Ltd. for any services rendered or for parting with any valuable right. The payment in this case admittedly was made to the holding company, Larsen and Toubro Ltd., for lending the services of some of its directors to manage the affairs of the assessee-company. Such payment, according to Dr. Balasubramanian, clearly falls within the purview of Section 40(c) of the Act.

7. We have carefully considered the rival submissions. The facts of the case are clear and uncontroverted. The assessee-company paid a total commission of Rs. 1,52,368 and Rs. 2,05,527 to Larsen and Toubro Ltd. in the previous years relevant to the assessment years 1981-82 and 1982-83, respectively, as directors' remuneration calculated at three per cent. of the net profits. Larsen and Toubro Ltd. was the holding company of the assessee-company, holding more than 50 per cent. shares of the assessee-company. It had lent the services of its directors to manage the affairs of the assessee-company. In lieu of the above services, the assessee-company paid the sums of Rs. 1,52,368 and Rs. 2,05,527 in the previous years relevant to the assessment years 1981-82 and 1982-83, respectively, to Larsen and Toubro Ltd.

8. The payment of the above amounts admittedly was made by the assessee-company to Larsen and Toubro Ltd. for the services of some of its directors lent to the assessee-company for managing its affairs. Such payment clearly falls within the purview of section 40(c) of the Act. The decision of the Supreme Court in *Commissioner of Income Tax, Bombay Vs. M/s. Indian Engineering and Commercial Corporation Pvt. Ltd.*, has no application to the facts of the present case. In that case, the controversy was about commission paid to the directors, in addition to their salary, at a percentage on the sales effected by them. It was in that context that the Supreme Court held that payment made to the directors by way of commission on sales effected by them did not fall within the purview of section 40(c) of the Act. The ratio of the above decision cannot apply to the payments made for the services rendered in managing the affairs of the

assessee-company. Similarly, the ratio of the decision of the Supreme Court in *Bharat Beedi Works (Pvt.) Ltd. and another etc. Vs. Commissioner of Income Tax*, is also not applicable to the facts of the present case. In that case, the controversy was regarding payments made by the assessee to a firm, the three partners of which were directors of the assessee-company, in consideration of valuable right parted with by the firm. The Supreme Court held that the payments having been made in consideration of the valuable right parted with by the firm in favour of the assessee-company, the said payments cannot be treated as payments made to the directors of the assessee-company, who were partners of the firm qua directors. The payments were made by way of consideration for allowing the assessee to use the valuable right belonging to them, i.e., the brand name. It was in that context that it was held that the payment did not fall u/s 40(c) of the Act. In the instant case, as indicated above, the payment was made to Larsen and Toubro Ltd., which is admittedly a company having substantial interest in the assessee-company, for the services of its directors lent to the assessee-company for the management of the assessee-company. This payment squarely falls within the purview of section 40(c) of the Act. The Tribunal, in our opinion, was justified in holding so. Accordingly, the questions referred to us are answered in the affirmative and in favour of the Revenue.

9. In view of the above finding of ours, we do not propose to deal with the controversy whether the above controversy is a facet of the controversy arising out of the questions referred to us or is a new controversy sought to be raised in the garb of the facet of the controversy involved in the questions referred to us.

10. These references are disposed of accordingly. There shall be no order as to costs.