

Srilal Kajaria Vs Jiwanmal Bhutoria**Appeal No. 131 of 1960**

Court: Calcutta High Court**Date of Decision:** March 13, 1968**Acts Referred:**

Income Tax Act, 1922 " Section 46(5A), 59

Citation: (1968) 1 CALLT 190 : (1969) 2 ILR (Cal) 248**Hon'ble Judges:** Masud, J; B.N. Banerjee, J**Bench:** Division Bench**Advocate:** R.C. Deb, S. Majumdar and Goutam Chakraborty, for the Appellant; P.P. Ghosh and B.C. Basack, for the Respondent**Final Decision:** Allowed

Judgement

BANERJEE J. - This is a reference u/s 66(1) of the Indian Income Tax Act, 1922. The assessment years involved are 1951-52 to 1955-56.

Before World War II, the assessee, Coal Shipments (Private) Ltd., was one of the companies, which used to export coal from India to Burma.

Amongst other such exporters, there was a company of the name of Messrs. H. V. Low & Co. Ltd. The war stopped such export. After the

cessation of hostilities, in 1946, it became possible to resume export to Burma. The exporters, including the assessee and H. V. Low & Co. Ltd.,

formed an association known as Coal Exporters and Charterers Association, inter alia, with the object of pooling up excess profits. The formation

of the association notwithstanding, the assessee and Messrs. H. V. Low & Co. Ltd. became potential rivals in coal export to Burma. Thereupon, it

is said, there was an understanding or an arrangement between the two on the following lines :

(a) Messrs. H. V. Low & Co. Ltd. will not export coal to Burma during the subsistence of the agreement;

(b) Messrs. H. V. Low & Co. Ltd. would place coal from their colliery at the ready disposal of the assessee for shipment to Burma and would

otherwise assist the latter in the export business; and

(c) the assessee will carry on the actual shipping business and pay to Messrs. H. V. Low & Co. Ltd. at 5 annas per ton (subsequently raised to

Re. 1-5 as per ton) of coal shipped to Burma.

According to the assessee, the last shipment of coal, under the above arrangement, was made in June, 1954. Thereafter, the arrangement came to

an end automatically because the Government of Burma began to look elsewhere for its coal requirements. Further, according to the assessee, it

made the following payments to Messrs. H. V. Low & Co. Ltd. under the aforesaid arrangement, during April 1, 1950, to March 31, 1955,

namely,

Rs.

1951-52 91,149

1952-53 1,77,898

1953-54 3,03,631

1954-55 3,32,355

1955-56 71,917

The amounts of payments are not in dispute and these payments have been taxed in the hands of Messrs. H. V. Low & Co. Ltd.

The assessee claimed the above payments as admissible business expenditure in the respective years of payments. The Income Tax Officer

disallowed the claim on the two-fold ground : (1) that there was no written agreement in proof of the arrangement and, as such, it was not possible

to say that the payments were made for the purposes of assessee's business, and (2) that assuming that the payments were made to keep off

Messrs. H. V. Low & Co. Ltd. from the Burma trade, they were payments to secure a monopoly and were not allowable as revenue expenses.

The Appellate Assistant Commissioner, on appeal by the assessee, connected with the Income Tax Officer and upheld the assessment.

On second appeal by the assessee, before the Appellate Tribunal, the same two points arose for consideration. The Tribunal noticed some

discrepancies in facts as stated on behalf of the assessee and the revenue. The Tribunal, thereupon, required the assessee to swear an affidavit in

support of the facts relied upon by it. Pursuant thereto, Sir Walter Michelmore of the assessee-company, affirmed an affidavit. He was also orally

examined before the Tribunal. The Tribunal remanded the case to the Income Tax Officer to verify the facts as stated in the affidavit and to report

back to the Tribunal accepted the report, in the absence of any objection thereto, and proceeded on that basis.

On the point as to whether the payments were made for the purposes of assessee's trade in terms of any agreement, the Tribunal found that there

was no agreement in writing and also that there was no resolution of the assessee's directions in confirmation of the alleged deal. Nevertheless, the

Tribunal held :

The entire evidence in point rests on the oral testimony of Sir Walter Michelmores, who is at present the chairman of Messrs. F. W. Heilgers &

Co. (P.) Ltd., the managing agents of the assessee-company. Sir Walter was examined by us on oath, as a court witness on his affidavit sworn in

pursuance of the Tribunals directive referred to above. Sir Walter stated that the terms were settled in the course of a verbal talk between himself

and Mr. Carpenter on behalf of the assessee-company and Mr. Indra Kumar Karnani, on behalf of Messrs. H. V. Low & Co. Ltd. He explained

that at the relevant time the great and infamous Calcutta killings of 1946 were going on and business had to be conducted under great stress and

strained no more businesslike relations were at that time practicable. Moreover, as stated by Sir Walter, the arrangement was treated as very

confidential and it was confined to only a few people at the top of the two organizations and these factors explain why there are no more

documents evidencing the deal than we actually find before us. In the absence of anything to the contrary, except mere suspicion, we see no reason

to disbelieve the sworn testimony of Sir Walter, who, as already stated, was examined before us as a court witness. It would be extremely

unreasonable to suppose that Sir Walter would perjure himself to bolster up a false case of one of the managed companies courting the risk of

prosecution.

The Tribunal further found that there were other materials showing that an agreement had in fact taken place and for that purpose relied on the

correspondence that passed between Sir Walter Michelmores (chairman of the managing agency of the assessee-company) and Mr. I. N. Karnani

(meaning director of Messrs. H. V. Low & Co. Ltd.). The Tribunal also found that the agreement was acted upon. Lastly, the Tribunal found that

payments were not made by the assessee to Messrs. H. V. Law & Co. Ltd. ex gratia but in the interest of the assessees business. The relevant

observation by the Tribunal is herein below set out.

The contention put forward of behalf of the department is that the assessee company was appointed as the agents of the Burma Government for

the supply of coal and, therefore, it had no reason to be afraid of any possible competition by Messrs. H. V. Law & Co. Ltd., or, for the matter of

that, by any other concern. In this connection, much stress is laid on the letter, dated the 7th August, 1946, written by Sir Walter to Shri Indra

Kumar Karnani in which it was stated that the assessee-company had been appointed, with effect from 1st August, 1946, as agents in India of the

Burma Government for the procurement and shipment of their coal requirements. The departmental representative contended that if, in point of

fact, the assessee-company had been appointed as the agents of the Burma Government for procurement and shipment of coal, the question of

competition by any other company in the export trade would not arise. Sir Walters attention was drawn to the above statement in the letter in the

course of his examination before the Tribunal and he said that he used the word agents in a rather loose sense and it appeared to us that the

witness had no clear idea about the legal implications of agency. It would not be correct, therefore, to lay under emphasis on the expression agents

used by Sir Walter in his letter of 7th August, 1946. Moreover, there are documents of unassailable authenticity to show that supply of coal and

coke to Burma was included in Open General Licence (O. G. L.) during the period from the 1st April to 31st March, 1953. ... and therefore,

competition might have arisen at any time. On behalf of the department our attention was drawn to a letter dated the 30th June, 1950, by Shri P. P.

Menon, Accounts officer in the Embassy of the Union of Burma (Trade Section), New Delhi, to the Deputy Coal Commissioner, 1, Council House

St., Calcutta, indicating therein the details of Burmas requirement of coal for the month of August, 1950. A copy of this letter was forwarded to the

assessee-company only and to no other traders. It is true that the fact that the intimation about the requirements of the Burma Government for coal

was not given to any other concern warrants an inference that the assessee-company alone had some sort of an authority for procuring and

supplying coal to the Government of Burma. But the letter supports the version of Sir Walter about the procedure then adopted by the Burma

Government for procuring coal from India. The procedure was that the Government of Burma through its Embassy in India intimated its

requirements for coal to the Coal Commissioner in India every month. It was the duty of the Coal Commissioner to meet such requirements. Sir

Walters attention was drawn in the course of his examination to the letter of Shri P. P. Menon, dated the 30th June, 1950, and he explained that at

the material time the assessee-company were also providing the ship for carrying coal of to Burma and, therefore, the purpose of sending Coal

Shipments Ltd., a copy of the letter in question was to give them an advance intimation of the tonnage in order that shipping could be arranged.

The explanation sounds plausible. Sir Walter has, moreover, stated in his affidavit (paragraph 10) that there was never any contract in writing

between the Government of Burma and Coal Shipments (Private) Ltd., whereby the latter were appointed to be the agents of the former for

procurement and or export of coal to Burma. In point of fact, the Income Tax Officer has in remand report, admitted that the word agent was used

by Shri Walter in his letter dated 7th August 1946, in a very loose sense....

That being so, there was always the possibility of competition by other traders in the field particularly when coal and coke was included in the

Open General Licence for export to Burma. Sir Walter has explained why the assessee-company was afraid of competition by Messrs. H. V. Low

& Co. Ltd. in particular, and not by any other company. He has said that Messrs. H. V. Low & Co. Ltd., who was one of the biggest pre-war

exporters of coal had in fact intimated their intention to enter into the Burma trade. The assessee-company regarded it as a possible threat to the

business secured by them and this was the driving motive which impelled it to enter into the arrangement with Messrs. H. V. Low & Co. Ltd. We

see no reason to reject the un rebutted testimony of Sir Walter in point. ... We are unable to accept the contention, therefore, that the payments

were made by the assessee ex gratia. We are of the view that the payments were made in pursuance of the said agreement in the interest of the

assessee's trade.... We are, in these circumstances, unable to accept the case of the department in point.

The Tribunal negated the contention that the payments were made to secure monopoly right to trade and as such were expenditure of capital

nature, with the following observation.

..... at the material time shipment of coal to Burma was under Open General Licence (O. G. L.) and it was open to all trader in the field to export

coal to that country. It is not, therefore, possible to hold that the payments in question were designed to secure a monopoly in that trade....

In the present case the assessee-company did not acquire the right to carry on the Burma trade by making the impugned expenditure; the

expenditure was made to carry on the trade in a more facile and more profitable manner. The assessee-company did not, obviously, derive any

advantage of an enduring character by such payments. The arrangement, arrived at verbally between the assessee and Messrs. H. V. Low & Co.

Ltd., was a temporary measure liable to be terminated at will by any of the two parties.

In the view taken, the Tribunal allowed the appeal and modified the assessment by exclusion of the sums claimed by the assessee as business

expenditure.

Aggrieved by the order of the Tribunal, the revenue obtained reference to this court of the following point :

Whether, on the fact and in the circumstances of the case, the payments made by the assessee to Messrs. H. V. Low & Co. Ltd. or their

nominees were of a capital nature and as such not allowable u/s 10(2) (xv) of the Income Tax Act, 1922 ?

It is no longer in dispute before us that there was an agreement between the assessee and Messrs. H. V. Low & Co. Ltd., on terms stated by the

assessee and that the payments in question were made thereunder. We are to see whether the expenditure was of capital nature and as such not

allowable as business expenditure u/s 10(2) (xv) of the India Income Tax Act.

The question of allocation to capital or income runs on fine lines of distinction and the distinction often proves puzzling. None of the tests laid down

in various authorities to distinguish between revenue expenditure and capital expenditure is exhaustive or universal. Each case must depend on its

own facts and a close similarity between one case and another is not enough, because even a single significant detail may alter the entire aspect. It

is not for nothing that Hidayatullah J. administered the caution in K. T. M. T. M. Abdul Kayoom v. Commissioner of Income Tax, that :

In deciding such cases, one should avoid the temptation to decide cases by matching the colour of one case against the colour of another.

We need, however, refer to one of the cases, cited before us on behalf of the revenue, namely, Assam Bengal Cement Co. v. Commissioner of

Income Tax, in which the Supreme Court reviewed the case-law and attempted to lay down certain workable tests, that is to say :

(1) Outlay is deemed to be capital when it is made for the initiation of a business, for extension of a business, or substantial replacement of

equipment;....

(2) expenditure may be treated as properly attributable to capital when it is made not only once and for all but with a view to bringing into

existence an asset or an advantage for the enduring benefit of a trade :....

The expression enduring benefit means that the asset or the right acquired must have enough durability to justify its being treated as a capital

assets....

The expression once for all is used to denote an expenditure which is made once and for all for procuring an enduring benefit to the business as

distinguished from a recurring expenditure in the nature of operational expenses.

(3) expenditure may be deemed to be capital when for the purpose of the expenditure any capital was withdrawn or, in other words, whether the

object of incurring the expenditure was to employ what was taken in as capital of the business.

The Supreme Court further observed in the above-mentioned case :

The aim and object of the expenditure would determine the character of the expenditure whether it is a capital expenditure or revenue

expenditure. The source or the manner of the payment would then be of no consequence. It is only in those cases where this test is of no avail that

one may go to the test of fixed or circulating capital and consider whether part of its circulating capital. If it was part of the fixed capital of the

business it would be of the nature of capital expenditure and if it was part of its circulating capital it would be of the nature of revenue expenditure.

These tests are thus mutually exclusive and have to be applied to the facts to each particular case in the manners above indicated. It has been

rightly observed that in the great diversity of human affairs and complicated nature of business operations it is difficult to lay down a test which

would apply to all situations. One has therefore got to apply these criteria one after the other from the business point of view and come to the

conclusion whether on a fair appreciation of the whole situation the expenditure is revenue expenditure in which latter even only it would be

deductible allowance u/s 10(2) (xv) of the Income Tax Act. The question has all along been considered to be a question of fact to be determined

by the Income Tax authorities on an application of the broad principles laid down above and the courts of law would not ordinarily interfere with

such findings of facts if they have been arrived at on a proper application of those principles.

To what we collect from the Supreme Court judgment referred to above, we need only add that when an expenditure is made or is undertaken for

the acquisition of an asset or advantage, in an outright manner and not subject to contingencies and when the consideration therefore together with

the obligation to pay the same is definitely and irrevocably fixed, then although the consideration may take the form of a named sum to be paid at

stated intervals, the payments is capital payment.

We do not propose to refer to other case-laws on the point, such as Pingle Industries Ltd. v. Commissioner of Income Tax, K. T. M. T. M. Abdul

Kayoom v. Commissioner of Income Tax and Gotan Lime Syndicate v. Commissioner of Income Tax, because they do not proceed on a basis

different from what we have hereinbefore summarised.

Turning again to the Assam Bengal Cement Company's case, on which great reliance was placed by the revenue, we find that the assessee-

company, formed with the object of carrying on business as miners of limestone and manufactures of cement, obtained for that purpose a lease of

certain limestone quarries from the Government of Assam for a period of twenty years for certain half-yearly rents and royalties. At the time the

lease was obtained the assessee had just been formed. Under the deed the lessor placed the assessee under certain special restrictions both as to

the actual operations of the business and as to the sale of its products. In addition to the rents and royalties the assessee agreed to pay the lessor

annually a sum of Rs. 5,000 during the whole period of the lease as a "protection fee" and in consideration of that payment the lessor undertook

not to grant any lease, permit or prospecting licence regarding limestone to any other party in respect of a neighbouring group of limestone quarries

without a condition that no limestone should be used for the manufacture of cement. The assessee also agreed to pay Rs. 35,000 annually for five

years as a "further protection fee" and the lessor in consideration of that payment gave a similar undertaking in respect of another group of quarries.

The question was whether in computing its profits the assessee was entitled to deduct the sums of Rs. 5,000 and Rs. 35,000 paid to the lessor u/s

10(2) (xv) of the Indian Income Tax Act, 1922. That question was answered in the negative. It was held that where before starting on its business

venture and by way of setting the stage for its business operation, a newly formed company took steps to ensure for itself certain condition of

security, which would last throughout the life of the project or during a substantial period and undertook to pay a consideration to the grantor of the

security, the expenditure although to be incurred periodically was capital expenditure. The question is whether the expenditure incurred by the

assessee was of the above type.

It was contended, on behalf of the revenue, that the expenditure was incurred to buy off competition by an experienced rival company and secure

a sort of monopoly business for coal export to Burma. In either event, it was submitted, the expenditure would be capital expenditure. Reliance

was placed in support of the proposition upon Collins v. Joseph Adamson (and vice versa) and Associated Portland Cement Manufacturers Ltd.

v. Kerr. We are not impressed by the argument. In the first place, at the material time, shipment of coal to Burma was under Open General

Licence and it was open to all coal merchants to export. Sir Walter Michelmores stated in his affidavit that Messrs. Macneill & Barry Ltd. and

Messrs. Turner Morrison & Co. Ltd. also used to export coal to Burma during this period. The Tribunal believed the statement. By neutralising

Messrs. H. V. Low & Co. Ltd., the assessee could not and did not secure monopoly right to export. Then again, the letter, dated August 7, 1946,

from Sir Walter Michelmores of the assessee-company to Mr. Indra Kumar Karnani of Messrs. H. V. Low & Co. Ltd. goes to show the motive

behind the arrangement. The material portion of the letter reads :

In accordance with our agreement in Coal Exporters and Charterers Association any excess profit will be credited to the pool and we will draw

the usual charge for shipping and handling. I hope, however, that this shipping charge will show some small profit after payment of expenses and I

propose that we should pay 50 per cent. of any such profit to you.

Apparently no written reply was received to this letter, Thereupon, Sir Walter Michelmores again wrote to Mr. Indra Kumar Karnani, the following

letter dated February 27, 1947 :

I cannot trace having received any reply from you to my letter dated 7th August, 1946, in which I suggested that you and we should share equally

in the Calcutta handling charges admissible to us for shipment of coal to Burma. Since the first shipment was in last August we have shipped a total

of 49,363 tons up to 31st December, 1946; your share of the 10 annas shipping fee on this tonnage would amount to Rs. 15,425-15 as and if you

confirm that the arrangement is acceptable to you I shall be pleased to forward to you a cheque for this amount.

Mr. Indra Kumar Karnani sent a reply to this letter, on March 2, 1947, accepting the proposal. The arrangement on the basis where the payments

to Messrs. H. V. Low & Co. Ltd., as believed by Tribunal, were made, was that :

(a) Messrs. H. V. Low & Co. Ltd., would assist the assessee in procuring coal for export to Burma, whenever asked.

(b) Messrs. H. V. Low & Co. Ltd. would not export coal to Burma during the substance of the arrangement.

The arrangement was not such as was likely to have an enduring beneficial effect. Like all agreements, with no certainty in duration, this

arrangement could at any time be terminated, revoked or be cancelled. The consideration for the arrangement was also not paid once for all,

related as the payments were to uncertain shipments to be made to Burma only the rate of payment was agreed upon and thereafter changed to a

higher rate. In our opinion, the motive behind the arrangement and the terms thereof did not envisage the creation of any monopoly trading right for

the assessee. There remained in the field other coal exporters to Burma. All that the arrangement secured for the assessee were certain temporary

advantages, namely :

(a) promise of assistance from Messrs. H. V. Low & Co. Ltd. in the matter of procurement of coal for export to Burma;

(b) promise from Messrs. H. V. Low & Co. Ltd. not to export coal to Burma by themselves.

Both the premises were delimited to uncertain duration of the arrangement which was terminable at will. The exclusion of Messrs. H. V. Low &

Co. Ltd. from the field of coal export to Burma was certainly of some commercial expediency to the assessee; otherwise no attempt should have

been made in that direction. But the expediency was limited, at the initial stage of resumption of coal trade with Burma, to the exclusion of a

competitor in coal shipment for some time at least, by a promise to them of a share in shipping charges. This may have been done with the object

of organising the assessee's own business more conveniently. The arrangement did not, in our opinion, bring about by capital advantage to the

assessee, according to the test laid down by the Supreme Court. If the payments were not capital expenditure, then regard being had to their

nature they must be taken to be expenditure incurred for carriage of business in a more facile and profitable manner. The expenditure must,

therefore, be attributable to revenue and allowable as deduction u/s 10(2) (xv) of the Indian Income Tax Act.

In the above view, the question should be answered in the negative and in favour of the assessee.

The assessee is entitled to costs.

K. L. Roy, J. - I agree.

Question answered in the negative.