(1989) 02 CAL CK 0044

Calcutta High Court

Case No: IT Reference No. 141 of 1979

Commissioner of Income Tax		APPELLANT
	Vs	
W. Howrah and Co. (P.) Ltd.		RESPONDENT

Date of Decision: Feb. 1, 1989

Acts Referred:

- Income Tax Act, 1922 - Section 10(2)(xi)
- Income Tax Act, 1961 - Section 256(1), 36(1)(vii)

Citation: (1989) 44 TAXMAN 409

Hon'ble Judges: Suhas Chandra Sen, J; Baboo Lall Jain, J

Bench: Division Bench

Advocate: B. Bagchi and M.L. Bhattacharjee, for the Appellant;

Judgement

Suhas Chandra Sen, J.
The following question of law u/s 256(1) of the income tax Act, 1961 ("the Act") has been referred by the Tribunal:

Whether, on the facts and in the circumstances of the case, and on the correct interpretation of the agreement dated 29th of March, 1961 between the assessee and New Central Jute Mills Co. Ltd. the Tribunal was right in holding that the assessee was entitled to the deduction of the loss of Rs. 72,141 as business loss in the assessment year 1961-62 ?

The assessment is in respect of the assessment year 1961-62, for which the relevant accounting year was the year ended on 31-3-1961. The facts found by the Tribunal, as stated in its order, are as follows:

One of the activities of the assessee was acting as principal broker for the supply of jute to jute mills. The assessee entered into contracts with the jute mills in that respect. One of

the jute mills was New Central Jute Mills Co. According to the contracts with the said jute mills the assessee agreed to shoulder the loss which the said jute mills might incur on account of the failure of the suppliers of raw jute to the said mills for whom the assessee had acted as brokers. In the year under consideration six parties, namely, (i) Sumermal Koshar, (ii) Sarkar Bailing, (iii) Anandilal Omprakash, (iv) Ramjidas Prahlajrai, (v) Ramjidas Jagannath, and (vi) Suraj Prasanna Chowdhary, failed to supply raw jute to the New Central Jute Mills Co. at the stipulated rates. The said jute mills purchased raw jute at higher rates and suffered losses on that account. The assessee later on entered into an agreement on 29-3-1961 with the New Central Jute Mills Co. According to that agreement the assessee agreed to pay 50 per cent of the losses suffered by the New Central Jute Mills Co. on account of the non-performance of the contracts by the said six parties. This agreement to bear 50 per cent of the loss was also subject to certain other conditions one of which was in case the New Central Jute Mills realised any amount from the said six parties, the realisation was to be shared equally by the assessee and the New Central Jute Mills. The assessee''s share of 50 per cent loss in respect of six parties amounted to Rs. 79,139. Subsequently, the New Central Jute Mills Co. was able to make recoveries from Sarkar Bailing and Anandilal Omprakash and the assessee''s share out of those realisations was Rs. 6,948. These realisations were made in the succeeding assessment years.

2. The ITO disallowed the claim of the assessee for deduction of loss, amounting to Rs. 79,139 paid by it to the New Central Jute Mills Co. The assessee preferred an appeal before the AAC. The AAC, however, affirmed the order of the ITO on this point. The assessee thereupon came, up in appeal to the Tribunal. The Tribunal, after considering the agreement by which the assessee had agreed to bear the losses suffered by jute company on account of failure of the suppliers to supply raw jute for whom the assessee had acted as a broker and after considering the subsequent agreement dated 29-3-1961, held that none of the six parties who had agreed to supply raw jute to the New Central Jute Mills Co. could be treated as debtors in respect of the losses suffered by the New Central Jute Mills Co. The Tribunal further held that the provisions of section 36(1)(vii) of the 1961 Act, or the provision of section 10(2)(xi) of the Indian income tax Act, 1922 could not be involved. The Tribunal held that the income tax authorities were wrong in their respective approaches not only factually but also legally. The Tribunal remanded the case to the AAC for reconsideration and passing a fresh order.

3. The AAC on remand observed "the payment of damages to the New Central Jute Mills Co. Ltd. was bona fide and was the direct consequence of the assessee carrying on business and acting as principal broker". The AAC allowed the claim of the assessee on this point. The ITO thereupon preferred an appeal to the Tribunal. It was submitted before the Tribunal that the payment of loss by the assessee was only an ex gratia payment as no liability to pay loss arose to the assessee. It was argued that the original agreement was to pay loss only in case the New Central Jute Mills Co. Ltd. obtained a decree for losses against the six defaulting parties. It was the case of the ITO before the Tribunal

that no decree was obtained for losses against the six defaulting parties and hence there was no liability on the assessee to pay any damages towards losses to the New Central Jute Mills Co. Ltd. Secondly, it was argued that even otherwise the loss did not relate to the year under consideration as no decree had been passed during the year. Therefore, the loss should not be allowed in this year. Lastly, it was argued that there was no liability to pay damages and no such liability arose on the basis of the original agreement and there was no justification for any payment and there is no question of loss having arisen in the facts of this case. It was also argued that on the basis of the agreement, the assessee became entitled to share 50 per cent of the realisations that might be made by the New Central Jute Mills Co. Ltd. from the defaulting parties and the loss would arise only if the assessee failed to recover its 50 per cent shares of losses from those parties and that the loss claimed by the assessee did not arise in the year under consideration.

4. The Tribunal, after consideration of the rival submissions ultimately held:

The New Central Jute Mills Co. Ltd. suffered the losses on account of failure of the above six parties to perform their part of the agreements for supply of raw jute to the said mills. The suffering of the losses by the said company did not depend upon the obtaining of any decree against them. The liability of the assessee to shoulder the losses arose when those six parties failed to perform their part of the agreement during the year under consideration. The provision for obtaining of decrees of losses against these parties by the New Central Jute Mills Co. Ltd. and the assignment thereof to the assessee was for the benefit of the assessee to enable it to recover the losses from those parties subsequently. It cannot, therefore, be said that the losses to the New Central Jute Mills Co. Ltd. did not arise in the year under consideration and the liability of the assessee to shoulder those losses also did not arise during the year. The assessee entered into the agreement with New Central Jute Mills Co. Ltd. on 29-3-1961 to reduce its liability for losses to 60 par cent otherwise it was required to shoulder the entire losses. The entering into the agreement of 29-3-1961 on the part of the assessee was on account of business expediency. The agreement dated 29-3-1961 entitled the assessee to share the realisation which might be made by the New Central Jute Mills Co. Ltd. subsequently equally but that did not in any way affect the liability of the assessee to bear 50 per cent of the losses suffered by the New Central Jute Mills Co. Ltd. Subsequent realisations, if any, can be taken into consideration in determining the income of the assessee in the year in which the realisations are made. In the circumstances of the case it cannot be said that the assessee did not suffer the losses claimed by it on the basis of the agreement dated 29-3-1961 with New Central Jute Mills Co. Ltd. The payment of losses by the assessee is also not ex gratia entered into by the assessee with the New Central Jute Mills Co. Ltd. We, therefore, affirm the order of the Appellate Assistant Commissioner.

There is no dispute that the assessee had paid the amount to New Central Jute Mills Co. Ltd. There is also no dispute that the six parties, introduced by the assessee-company had committed default. The assessee was acting as broker. All these transactions have

taken place in course of brokerage business of the assessee-company. The transactions are all incidental to the carrying on of the brokerage business. The real question is whether the amount was spent by the assessee in course of carrying on business as broker. On the facts of this case, it cannot be urged that this was not a commercial transaction. Having regard to the nature of the business activities of the assessee and the nature of agency business. The amount of loss, incurred during course of such business activities must be allowed as deductible in computing the income of the assessee''s business. If any amount is recovered subsequently, then that will have to be treated as revenue receipt of that year.

5. Next it was argued that such payment by the assessee will be treated as capital receipt in the hands of the New Central Jute Mills Co. Ltd. Even if this payment is treated as capital receipt by the jute mills, for the assessee it was revenue expenditure, incurred in course of carrying on of the business. The loss fell upon the assessee, in course of trading. In the facts of this case, we see no reason why this amount is not to be allowed as deduction while assessing the income of the assessee.

6. The question is, therefore, answered in the affirmative and in favour of the assessee. There will be no order as to costs.

Baboo Lall Jain, J.

I agree.