

Juggilal Kamlapat

Vs

Commissioner of Income-Tax U. P.

Civil Appeals Nos. 968 and 969 of 1967

(J. C. Shah, V. Ramaswami, A. N. Grover JJ)

04.09.1968

JUDGMENT

RAMASWAMI J. -

These appeals are brought by special leave from the judgment of the a Allahabad High Court dated July 10, 1962, in Income- tax Miscellaneous Cases Nos. 255 and 256 of 1955.

The appellant, M/s. Juggilal Kamlapat, hereinafter called the "assessee", was a registered partnership firm having the following constituents :

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Names of the partners

shares

1. Shri S. M. Bashir	49 per cent.
2. Sri Padampat Singhania	17 per cent.
3. Shri Lakshmipat Singhania	17 per cent
.4. Sri Kailashpat Singhania	17 per cent.

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Total

100 per cent

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The shareholding of the three Singhanian brothers was 51 per cent. constituting a majority of the shareholding in the partnership firm. The partners of the said firm floated a company, namely, M/s. J. K. Iron and Steel Company Ltd., the constitution of which was that the three Singhanian brothers and their wives had 166 shares while Sri S. M. Bashir and his wife had 42 shares. In consideration of the fact that the assessee firm promoted the company the assessee was appointed the managing agent of M/s. J. K. Iron and Steel Company Ltd. for a period of 25 years under a managing agency agreement dated December 15, 1938. It was provided in this agreement that the assessee will continue to be the managing agent until it resigned or it was removed from its office of managing agency by a majority of 3/4th of the shareholders of the managed company. According to the terms of the agreement the managing agent's remuneration was Rs. 1,500 per month and a commission of 10 per cent. on net profits of the company after deduction.

Paragraph 2(m) : "It shall be lawful for the firm to assign their officers as agents and all the rights and obligations as such agents and in the event of assignment, the assignee or assignees shall be deemed to have been appointed agents of the company with like powers and authorities remuneration and emoluments and subject to like terms and conditions as are herein contained....."

Paragraph 2(c) : "The firm may at their option from time to time lend and advance to and for the use of the company, money on interest to any extent as they may like, the same to run at a minimum rate of five per cent. per annum provided that if the bank rate prevailing at the date of advance is higher than five per cent. The firm may charge interest at one per cent. above the bank rate."

On August 12, 1943, a meeting of the board of directors of the managed company was held. The directors present were : (1) Sri Padmapat Singhanian, (2) Sri Lakshmi Pat Singhanian and (3) Sri S. M. Bashir with Sri Padmapat Singhanian in the chair. At this meeting a letter dated August 3, 1943, from M/s. Juggilal Kamalpat, Bankers, the financiers of the managed company, asking for re-payment of advances made by the financier to the company exceeding Rs. 5 lakhs was discussed. Sri S. M. Bashir pointed out that the managing agents were under no obligation to provide finance for the company at the latter's direction. It was the option of the firm to provide or not to provide finance and also to determine the extent of the advance. Sri Padmapat Singhanian thereupon pointed out that even though the matter of providing finance might be at the discretion of the managing agents "it was the usual practice with companies under the management of the managing agents to obtain their finance from the managing agents". According to

The constitution of M/s. J. K. Commercial Corporation was as follows :

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'A' class ordinary 'B' Class ordinary shares of Rs. 100 shares of Rs. 10 each. each. Rs.

Rs.-----I. (a) Sri Padmapat
1,750 5,000(b) Lady Ansuiya Singhanian, wife of Sri Padmapat (Natural guardian of

her minor son, Gopal Hari 750(c) Lady Ansuiya Singhania (Natural guardian of her minor son, Ch. gaurhari) 500II. (a) Lala Kailashpat Singhania 1,750 500(b) Lala Kailashpat (Natural Guardian of his minor son, Vijaipat) 600III. (a) Lala Lakshmiapat Singhania 500 1,000(b) Shrimati Pushpawathi Devi, wife of Lakshmiapat (Natural guardian of her minor son, Harishanker) 750IV. (a) Lala Radhakrishan Singhania, uncle of Sri Padampat 70(b) Lala Purshottamdas Singhania, cousin of Sri Padampat 100(c) Lala Sohan Lal Singhania, cousin of Sri Padampat 1,000 2,000V. (a) Sri. P. D, Chandra Rana, P. A. to Sri Padampat 100 100(b) Shri Gopikishan Jaipuria, Munist of J. K. Kanpur (Kothi) 10(c) Shri S. M. Bashir, director J. K. Iron and Steel Co. Ltd. 100(d) Lala S. D. Garg 100(e) Lala Sital Prasad, director of J. K. Woollen Mills 500 1,900 -----Total 8,580 15,000 -----
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It is apparent from this constitution that the shares of the three Singhania brothers, their wives and children in J. K. Commercial Corporation Ltd. were 6,600 'A' class ordinary shares out of 8,580 and 11,000 out of 15,000 'B' class ordinary shares. The remaining shares were allotted to the personal assistant to Sri Padmpat Singhania, a munim of the firm of Juggilal Kamapat, a director of the managed company, one S. D. Garg and to a director of an allied concern.

M/s. J. K. Commercial Corporation Ltd. were appointed managing agents for a period of 20 years, renewable thereafter for a term not exceeding 20 year at a time. The remuneration was to be an officer allowance of Rs. 1,000 per month, a commission of 10% on the net annual profits of the company and a commission of 2 1/2% on the gross sales of the products of the company. Paragraph 8 of the managing agency agreement states :

"The managing agents shall from time to time lend and advance to and for the use of the company such moneys as may from time to time be required by the company up to an amount not exceeding Rs. 20,00,000 at any one time, but they may, however at their option lend and advance even more money if so required by the company. The company shall pay to the managing agents, interest on moneys so lent and advanced at a rate to be mutually agreed upon from time to time."

The amount of Rs. 2 lakhs compensation paid to the assessee-firm was worked out on the basis of 5 preceding years' profits of the managing agency from November 1, 1938, to October 31, 1943. The sum of Rs. 2 lakhs was paid to the assessee on October 31, 1943. The amount was claimed by the assessee as compensation for loss of office not liable to tax under the Income-tax Act as a capital receipt. The receipt of this sum of Rs. 2 lakhs, though incorporated in its books by the assessee, was not disclosed at the time when the assessment was originally made against it on April 6, 1945. Later on who it was discovered that the assessee had received the sum from the managed company the assessment was reopened under section 34 of the Income-tax Act and proceedings were also taken under section 15 of the Excess Profits Tax Act for the corresponding chargeable accounting period and the amount was included in the total computation of the assessee's business income. The assessee challenged these assessments on the ground that

"Whether there was material on which the Tribunal could hold that the receipt of Rs. 2,00,000 by the assessee was revenue receipt liable to tax under the Income-tax Act and the Excess Profits Tax Act ?"

By its judgment dated July 10, 1962, the High Court answered the question against the assessee and

in favour of the Commissioner of Income-tax, U. P. the High Court took the view that the amount of Rs. 2 lakhs was received by the assessee "by virtue of its office" and "relate to the work of the managing agency" even though the payment was collusive and there was no real termination of the managing agency agreement. It was points doubt by the High Court that the collusive payment could not have been made if the assessee had not been the managing agent of the managed company and the managing agency business of the assessee was exploited for getting the amount of Rs. 2 lakhs.

On behalf of the appellant Mr. Sukumar Mitra stressed the argument that the High Court failed to appreciate that the assessee-firm was a distinct legal entity and was different from J. K. Commercial Corporation which was a separate legal entity in the eye of law and the mere fact that the shareholdings of the partners of the assessee- firm in the J. K. Commercial Corporation was of a considerable preparation should not have led the High Court to the inference that the rights of the assessee-firm were not destroyed, sterilized or lost on account of the transaction. To put it differently, the contention of the appellant was that the High court was not entitled to go behind the legal form of the transaction and to find out what was the substance. We are unable to accept the argument of Mr. Sukumar Mitra as correct. In the present case the Appellate Tribunal has found that the transaction of termination of the managing agency was a colourable transaction and the real purpose was to hand over a sum of Rs. 2 lakhs

We proceed to consider the next argument addressed on behalf of the assessee, viz., that the amount of Rs. 2 lakhs cannot be held to be a revenue receipt even though the transaction of termination of the managing agency was collusive and the intention of the parties was to evade income-tax. The argument put forward on behalf of the appellant was that, even if the transaction was collusive and not genuine, it was legally permissible for the assessee to arrange its affairs in such a way as to avoid the incidence of tax. It was argued that even upon the facts found by the Appellate Tribunal the amount of Rs. 2 lakhs paid to the assessee-firm was not taxable as income in its hands because there was an actual termination of the first managing agency agreement and the amount of Rs. 2 lakhs was actually paid to the assessee-firm for the termination of the managing agency contract. The argument was stressed that the assessee firm had no other business activity except the managing agency in question and that the manag

On behalf of the appellant it was said by Mr. Sukumar Mitra that a mere intention on the part of the assessee to evade income-tax will not nullify an otherwise lawful transaction. But we have already shown that the Appellate Tribunal has found in the present case that the transaction of termination of the managing agency contract was sham transaction and was stage-managed merely with a view to evade income- tax and the real intention was that the three Singhanian brothers should continue to carry on the managing agency in a dominant capacity in the guise of a limited company and there was in fact no loss of office or destruction of profit yielding apparatus. Reference should be made in this connection to the following observations of Lord Greene M. R. in *Lord Howard De Walden v. Commissioners of Inland Revenue* :

"But even if the only alternative to Mr. Tucker's constructions, we are not prepared to say that it is necessarily as unjust as he contends. The section is a penal one and its consequences, whatever they may be, are intended to be an effective deterrent which will put a stop to practices which the Legislature considers to be against the public interest. For years a battle of maneuver has been waged between the Legislature and those who are minded to throw the burden of taxation off their own shoulders on to those of their fellow subjects. In that battle the Legislature has often been worsted by

the skill, determination and resourcefulness of its opponents, of whom the present appellant has not been the least successful. It would not shock us in the least to find that the Legislature has determined to put an end to the struggle by imposing the severest of penalties. It would not shock us in the least to find that the Legislature has determined to put an end to the struggle by imposing the severest of penalties.

We therefore reject the argument of Mr. Sukumar Mitra on this point.

For the reasons expressed, we hold that the judgment of the Allahabad High Court dated July 10, 1962, is correct and these appeals must be dismissed with costs-one set of hearing fee.

Appeals dismissed.

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