Commissioner of Income-Tax, Andhra Pradesh

Vs

Dhanrajgirji Raja Narasingirji

Civil Appeals Nos. 1653 and 1654 of 1970

(K.S. Hegde, P. Jagmohan Reddy, H.R. Khanna JJ)

07.03.1973

JUDGMENT

HEGDE J. -

1. These are appeals by special leave. They arise from a reference under Section 66(1) of the Indian Income-tax act 1922. In order to properly appreciate the decision of the High Court it would be convenient to set out the material facts the very outset.

2. The assessee, an individual derived during the accounting years ending on October 21, 1949 and November 9, 1950 - the relevant assessment years being 1950-51 - considerable income from various sources in Hyderabad as well as in other places. In 1935 the assesses had promoted a public limited company called 'Dhanraj Mills Ltd.' at Bombay. The assessee was appointed as its managing agent for the period of 50 years. He was also appointed as a permanent director and Chairman of the board of Directors. In 1937 the Company got into financial difficulties. Hence the assessee invited the assistance of one Ramgopal Ganpatrai who agreed to bring in the necessary finance. A tripartite agreement was entered into between the assessee the Company and the said Ramgopal Ganpatrai. Under that agreement it was provided that the assessee should give up the managing agency and the Company should appoint Ramgopal Ganpatrai or his nominee as the new managing agent. A selling agency agreement was also to be entered into between the Company and Ramgopal Ganpatrai or his nominee. As per that agreement the assessee was to be paid certain office allowance and a share in the managing agency commission by way of compensation. Under that agreement, he also became entitled to 3/8th share of the selling agency commission as may accrue under the proposed selling agency agreement. It was further provided that in case either the managing agency agreement or the selling agency agreement came to be terminated, the assessee, at his option, would be entitled to resume the managing agency as well as the selling agency. In pursuance of the aforementioned tripartite agreement, the managing agency agreement and the selling agency agreement were executed by the Company. Accordingly, Ramgopal Ganpatrai became the managing agent as well as the selling agent of the Company. This position continued for some years. In 1943, Ramgopal Ganpatrai floated two private limited companies and assigned the managing agency and the selling agency respectively to those two companies. The assessee's consent thereto was also obtained, as stipulated in the agreement. In 1946, Ramgopal Ganpatrai moved a resolution for the removal of the assessee as the Chairman of the Board of Directors of the Company on the ground that he had committed offences under Section 86F of the Indian Companies Act. That resolution was accepted and the assessee was removed from his office of the Chairman of the Board of Directors. In 1947 the selling agency was surrendered by the private company floated by Ganpatrai, by it did not revert to the assessee as provided in the original tripartite agreement. The assessee, thereupon, instituted a civil suit seeking his reinstatement as the Chairman of the Board of Directors of the Company. In

that suit he also sought to establish his right to the selling agency. Therein, he alleged that the Company had in collusion with Ramgopal Ganpatrai sought to oust him from his office of the Chairman of the Board of Directors and further prevented him from getting the selling agency. During the tendency of that suit, the assessee lodged a complaint with the police alleging misappropriation of the Company's funds as well as other fraudulent acts on the part of Ramgopal Ganpatrai while managing the Company. He also made other allegations with which we are not concerned in this case. In pursuance of that complaint, the Government instituted a criminal case against Ramgopal Ganpatrai. After obtaining the permission of the Court and with the consent of the Government, the assessee employed his own lawyers to prosecute that case. The prosecution culminated in the conviction of Ramgopal Ganpatrai. The conviction was upheld by the High Court on June 22, 1951. While the civil litigation as well as the criminal appeal were pending, the assessee and Ramgopal Ganpatrai entered into a settlement. Under the settlement Ramgopal Ganpatrai gave up the managing agency and further affirmed the right of the assessee to the selling agency. The selling agency commission was made payable to the assessee and the same was taxed in the assessment year 1948-49.

3. The amounts spent by the assessee in connection with the aforementioned civil and criminal litigations during the relevant previous years were claimed by him allowable deductions under Section 10(2)(xv). We are not now concerned with the amount spent for the civil litigation. That has been given deduction. So far as the amount spent for criminal litigation is concerned, the Tribunal came to the conclusion that in assessment year 1949-50, the assessee had spent a sum of Rs. 9,836 and further in the assessment year 1951-52, he had spent a sum of Rs. 57,066. It further came to the conclusion that the assessee expended of all these amounts for the purpose of the business. The Tribunal opined that the criminal case was instrumental in bringing about the compromise. The effect of the Tribunal's findings is that the assessee incurred the expenditure in question for the purpose of the business. The question for consideration is whether such and expenditure is deductible under Section 10(2)(xv). Section 10(1) provides for the assessment of income from business. Section 10(2) provides for certain deductions from that income Section 10(2)(xv) provides for the deductions of :

> "any expenditure (not being an allowance of the nature described in any of the clauses (i) to (xiv) inclusive, and not being in the nature of capital expenditure of personal expenses of the assessee) laid out or expended wholly and exclusively for the purpose of such business, profession or vocation."

4. The Tribunal has found that the expenditure in question had been incurred by the assessee; it was a bona fide expenditure and it was incurred for the purpose of business. From the circumstances of the case it is clear it was wholly and exclusively expended for the purpose of the business though the Tribunal did not specifically say so. After giving those findings, strangely enough, the Tribunal held that only one-third of that expenditure should be considered as having been expended wholly and exclusively for the purpose of business in question. The Tribunal's decision as to appointment of the expenditure appears to be on the basis of estimate. The Tribunal was not justified under the circumstances of the case, in apportioning the expenditure incurred. But the assessee did not complain against the finding. At the instance of the commissioner of Income-tax, the Tribunal submitted the following two questions to the High Court :

> "(1) Whether, on the facts and in the circumstances of the case, any part of the expenditure incurred by the assessee in connection with the criminal proceedings initiated and conducted under Section 10(2)(xv) of the Indian Income-tax Act, 1922 ?

and

(2) If the answer to question No. 1 is in the affirmative, whether there is any basis for estimating such allowable part of expenditure at one-third of the total ?"

5. The High Court, while accepting the conclusion reached by the Tribunal that the expenditure in question was incurred for the purpose of business carried on by the assessee, at the same time opined that the entire expenditure incurred should have been given deduction. It advised the Tribunal accordingly. But, at the same time, it asked the Tribunal to re-examine the exact amount expended by the assessee in connection with the criminal litigation.

6. In our opinion, the High Court was not justified in going beyond the questions referred to it. The assessee did not move the Tribunal to refer any question of law to the High Court. He appears to have accepted the decision of the Tribunal. The questions referred to the High Court must be understood in the light of the facts and circumstances of the case. The finding of the Tribunal as to the amount spent in connection with the criminal litigation is a finding of fact. That finding was not challenged. What was challenged under question No. 2 was the basis of apportionment of that expenditure. All that the High Court had to consider was whether the expenditure in question was deductible under Section 10(2)(xv) and whether the tribunal was justified in allowing one-third of the amount spent as deductible expenditure. It was not open to the High Court to sit as a court of appeal and examine the entire case afresh. Its duty was merely to advise the Tribunal on the questions referred to it.

7. Now, coming to the questions referred, it was urged by Mr. Ahuja, learned Counsel for the revenue, that an expenditure incurred in connection with a criminal case cannot be considered as an expenditure coming within the scope of Section 10(2)(xv) of the Act. He contended that an expenditure incurred in connection with a civil litigation can be given deduction to; if the conditions prescribed in Section 10(2)(xv) are satisfied, but no such deduction can be given if any expenditure is incurred in connection with a criminal case. We find no support for this connection from the language of Section 10(2)(xv). That provision does not make any distinction between civil litigation and criminal litigation. In fact, expenses incurred in connection with litigation are not separately dealt with under that provision. In our opinion, it makes no difference whether the proceedings are civil or criminal. All that the Court has to see is whether the legal expenses were incurred by the assessee in his character as a trader, in other words, whether the transactions in respect of which proceedings are taken arose out of and was incidental to the assessee's business. Further we have to see whether the expenditure in question was bona fide incurred wholly and exclusively for the purpose of business : see Commissioner of Income-tax v. Birla Cotton Spinning and Weaving Mils Ltd. ((1972) 1 SCR 283 : (1971) 82 ITR 166) It is true that in some of the cases this Court has held that an expenditure incurred by an accused assessee to defend himself against a criminal charge did not fall within the scope of Section 10(2)(xv). Those decisions were rendered on the facts of those cases. That is not the position in this case. On the findings arrived at by the Tribunal, it is clear that the assessee had incurred the expenditure in question for the purpose of his business. The learned Counsel for the revenue urged that there was no necessity for the assessee to incur that expenditure, as the prosecution was launched by the Government. It was not urged, and it could not have been urged, that the expenditure was not bona fide incurred. The Tribunal has come to the conclusion that the expenditure in question has been incurred. The contention that, as the Government was conducting the prosecution, there was no necessity for the assessee to engage his own lawyers is not substantial. It was for the assessee to decide how best to protect his own interest. It was the duty of the assessee to see that the prosecution was properly conducted. He was interested in successfully

prosecuting the case. The fact that he did not leave the carriage at the case in the hands of the prosecuting agency of the Government is no ground for disallowing the expenditure. It is not open to the department to prescribe what expenditure an assessee should incur and in what circumstances he should incur that expenditure. Every businessman knows his interest best. So far as the apportionment is concerned we are not told why we should not consider the same as a reasonable estimate.

8. For the reasons mentioned above, we vacate the order make by the High Court and in its place we answer the questions referred to in the affirmative and in favour of assessee. The appeal is decided accordingly. Parties to bear their own costs.

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