C. I. T., Punjab, Haryana, J And K, H. P. and Union Territory of Chandigarh

Vs

M/S. Panipat Woollen and General Mills Co. Ltd., Chandigarh

Civil Appeals Nos. 622 and 623 of 1971

(R.S. Sarkaria, Syed M. Fazal Ali JJ)

21.01.1976

JUDGMENT

FAZAL ALI, J. -

1. These are appeals by the Revenue by special leave against the order of the High Court of Punjab & Haryana dated January 20, 1970 answering the questions referred to the High Court by the tribunal in favour of the assessees/respondents and against the Revenue. The appeal arises in the following circumstances.

2. M/s. Panipat Woollen & General Mills Co. Ltd. - hereafter referred to as 'the assessee company' had two departments - (1) for spinning of yarn from raw and waste wool and (2) for spinning of yarn from imported wool tops. The second department which carried on the operations of spinning of yarn from imported wool tops was started sometime in the year 1952. Weaving operations were, however, carried on in both these departments. One of the departments was known as M/s. Panipat Woollen Mills, Kharar while the other one was known as M/s. Navin Woollen Mills. It is said that the assessee company was running at a constant loss as a result of which in 1952 the assessee company decided to instal a plant for manufacturer of worsted yarn from imported wool tops by raising a loan of Rs. 7 lakhs from the Industrial Finance Corporation. The plant went into production in September 1952. The assessee company appointed M/s. Murlidhar Chiranjilal as the sole selling agents for the worsted yarn on payment of 2% commission. Subsequently on December 15, 1953 the assessee company entered into an agreement with M/s. Saligram Premnath under which the latter were appointed as the sole selling agents on certain specified conditions, the important of which being that the agents were to finance the assessee company to the extent of Rs. 2,50,000 and the assessee company agreed to pay 6% interest on the advances to be made by the agents and further agreed to pay 2% commission on the net proceeds of sales of goods in India. Before expiry of this agreement, another agreement was entered into by the assessee company with the agents on October 20, 1955 under which the agents were to get 6% interest on all the advances made by them. 1 1/4% commission on net sales and 50% commission on net sales of the worsted plant. What is more was that the agents agreed to a deduction of 50% of the loss incurred by the assessee company from their remuneration. There were a number of other conditions with which we shall deal later. The selling agents M/s. Saligram Premnath advanced a sum of Rs. 6,26,847 and Rs. 8,71,573 and received Rs. 37,157 and Rs. 73,787 as 50% commission on the net profits of the worsted plant in the course of two years, namely, assessment years 1956-57 ending on March 31, 1956 and 1957-58 ending on March 31, 1957. The assessee company accordingly in its return for the year 1956-57 claimed the amount of Rs. 37,157 and Rs. 73,787 for the assessment year 1957-58 as a deduction under the provisions of Section 10(2)(xv) of the Income-tax Act, 1922. The case of the assessee was that the two amounts mentioned above being in the nature of commission paid to

the selling agents would be deemed expenses incurred by the company in order to earn profits and would, therefore, fall within the ambit of section 10(2)(xv) of the Income-tax Act, 1922 - hereafter referred to as 'the Act'. The Income-tax Officer, however, disallowed the deduction and held that the deduction claimed was actually a division of profits after the profits had come into existence and had been ascertained, and therefore could not be claimed as a valid deduction under the provisions of the Act. The assessee company went up in appeal to the Appellate Assistant Commissioner who accepted the pleas of the assessee company and held that the payment was a permissible deduction as it was incurred for the purpose of the assessee's trade in order to facilitate the business of the assessee. The Revenue then went up in appeal before the tribunal which after considering the facts and the law on the subject upheld the contention of the Revenue and held that the sums in question were not legal deductions as contemplated under Section 10(2)(xv) of the Act but amounted to application of profits after they were earned. The tribunal further held that the agreement dated October 20, 1955 amounted to a joint venture for the distribution of profits between the assessee company and the selling agents after the profits were ascertained. The assessee company then approached the tribunal for making a reference to the High court and the tribunal accordingly referred the following two questions to the High Court for its opinion :

1. Whether on the facts and in the circumstances of the case, the tribunal rightly held that the sum of Rs. 37,157 and Rs. 73,787 were chargeable to tax in the hands of the assessee company in the assessment years 1956-57 and 1957-58 respectively ?

2. Whether on the facts and in the circumstances of the case, the tribunal rightly disallowed the assessee company's claim for deduction of the payment of Rs. 37,157 and Rs. 73,787, under Section 10(1) and Section 10(2) (xv) of the Income-tax Act, 1922, in the assessment years 1956-57 and 1957-58 respectively ?

The High Court by its judgment dated January 20, 1970, answered both the questions in favour of the assessee company and held that the payments in question amounted to a legitimate deduction under Section 10(2)(xv) of the Act, and the tribunal was wrong in disallowing the same. Thereafter the appellant moved the High Court for grant of leave to appeal to the Supreme Court which having been rejected the appellant filed a petition for special leave. The special leave having been granted, the appeal is now before us.

3. The High Court in reversing the order of the tribunal mainly relied on what it described the surrounding circumstances under which the alleged payment were made to the selling agents by the assessee company as spelt out from the agreement entered into by the assessee company with the selling agents. The main point which was argued before the tribunal as also before the High Court was that the cumulative effect of the interpretation of the various clauses of the agreement dated October 20, 1955 unmistakably revealed that in the garb of an agency the parties entered into a joint venture for distributing the net profits after being ascertained between themselves and that is why there was an express provision in the agreement by which the agents agreed to share the losses to the extent of 50% which were to be deducted from the remuneration payable to the agents. The tribunal held that the agreement amounted to joint venture resulting in division of net profits and therefor the amount paid to the agents could not be claimed by the assessee company as a deduction under Section 10(2)(xv) of the Act, as it was not incurred for the purpose of the business or for earning profits. The High Court held that the mere fact that the agents agreed to share the profits. The High Court held that the mere fact that the agents agreed to share the profits and the losses would not take the case of the assessee beyond the ambit of Section 10(2)(xv) of the Act in order to show that the payments made to the agents were not expenses incurred for the purpose of the business. The High

Court laid special emphasis on the fact that the Revenue could not examine the question of the commercial expediency of the businessman to incur expenses or earn profits in a particular manner. The High Court accordingly found that the agreement per se was a contract of agency and not a joint venture and accordingly the High Court accepted the plea of the assessee company.

4. In support of the appeal Mr. Ahuja, the learned standing Counsel for the Revenue submitted the following two points before us :

(1) In the first place it was submitted that there being an express provision in the agreement dated October 20, 1955 by which the agents agreed to share losses which was a provision peculiar to the present transaction and was not at all covered by any authority cited before the tribunal or the High Court, that itself was proof positive of the fact that the transaction amounted to a joint venture with a view to division of profits; and

(2) it was argued that the High Court had exceeded its jurisdiction in travelling beyond the agreed statement of the case framed by the tribunal and had relied on certain materials which were not at all found by the tribunal in its order nor were those materials mentioned in the statement of the case.

5. Mr. A. N. Goyal, Counsel for the assessee company has, however, submitted that the view taken by the High Court is absolutely correct and the facts of the present case are clearly covered by the decision of this Court in Dharamvir Dhir v. C.I.T., Bihar & Orissa ((1961) 42 ITR 7 : (1961) 3 SCR 359 : AIR 1961 SC 668). A number of the other cases have also been cited at the Bar and we shall refer to the same after marshalling the facts found in the present case.

6. Before coming to the facts it may be necessary to mention that there can be no dispute with respect to the two important propositions :

(1) that in order to fall within Section 10(2)(xv) of the Act the deduction claimed must amount to an expenditure which was laid out or expended wholly and exclusively for the purpose of the business, profession or vacation. This will naturally depend upon the facts of each case.

(2) that in order to determine the question of reasonableness of the expenditure, the test of commercial expediency would have to be adjudged from the point of view of the businessman and not of the Income-tax Department.

With this preface we now proceed to deal with the facts of the present case on the basis of which the questions of law referred to the High Court and answered in favour of the assessee company arise.

7. To begin with, it is conceded by the learned standing Counsel for the Revenue that the assessee company was running at a loss as a result of which it had to raise a loan of several lakhs of rupees from the Industrial finance Corporation. It was perhaps for this reason that the assessee company entered into an agreement with the new selling agents M/s. Saligram Premnath who were prepared to give to the assessee company better and more profitable terms. The main question to be determined is as to whether or not the agreement dated October 20, 1955 read as a whole amounts to a joint venture for the purpose of division of profits. In order to decide this question it may be necessary to refer to some important portions of the second agreement which alone is relevant for the purpose of deciding this point. We might mention, however, that so far as the first agreement is concerned the terms thereof do not make out a case of joint venture but appear to be in consonance with the agreement being one of an agency simpliciter. It is the second agreement that in our opinion appears to change the entire complexion of the case. This agreement is set out at p. 17 of the

paper book and consists of ten main clauses. The agreement was to enure for a period of two years to commence from January 1, 1956 or the date on which manufacturing actually starts under the agreement whichever is later. This is provided in Clause 2 of the agreement. It was further provided that the period of the agency could be extended further by mutual consent. Clause 3(ii) runs thus :

Programme for the manufacture of goods will be made from time to time by the company in consultation and with the consent of the Agents.

It may be noticed that this clause requires not only consultation with the agents for the programme of manufacture of goods but a tacit consent of the agents. In other words, if the agents withheld their consent, they could veto the programme of manufacture. Such a limitation placed on the power of the assessee company does not appear to us to be in consonance with a pure and simple contract of agency. Clause 6 which deals with financial arrangements may be extracted thus :

(i) The Agents shall invest full amount for the working of the Worsted Plant to the full possible capacity beginning from the purchase of tops to the completion of the yarn sales including wages, power, stores, and repairs and maintenance, etc. Such investments and expenses incurred on tops, manufacturing, bank charges, transport, insurance and octroi will be debited to the account of the company.

(ii) Before the beginning of the arrangements under this Agreement, the Machinery of the Worsted Plant will be overhauled and similarly before this arrangement ends the Machinery will be overhauled.

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(viii) In case of any loss or damage to the tops or goods in transit or in godowns, the same will be debited to the account of the worsted Plant.

(ix) The accounts of the Worsted Plant will be maintained separately in an office situated near the Worsted Plant and the Agents will have free access to the account books.

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Sub-clause (i) clearly contemplates that the agents would have to make full and complete investment for the working of the worsted plant to the fullest possible capacity including wages, power, stores, repairs and maintenance etc. This provision appears to be more in consonance with the terms of a person who is a partners in a venture rather than one who is a mere agent. Furthermore, sub-clause (ii) provides that before the agreement starts the machinery of the worsted plant would be overhauled and would be again overhauled before the agreement ends. This provision also has its own importance and appears to be beyond the role of the selling agents simpliciter. Sub-clauses (viii) and (ix) extracted above clearly show that the damage of the tops or goods in transit would have to be debited to the account of the worsted plant and such accounts would have to be maintained separately. The obvious object is that the agents would be in a position to ascertain the net profits and control the working of the worsted plant. Clause 7 is the most important clause of this agreement, which, in our opinion, clearly shows that the agreement in essence and in purport is a sort of a partnership or a joint venture rather than a contract of agency. Sub-clause (i) of Clause 7 runs thus :

7. Commission - (i) The Agents shall be allowed a commission at 1 1/4% (one and a quarter per

cent) on the net proceeds of sales of all goods. Such commission shall be chargeable upon money actually credited to the Company, and not on outstanding debts, if any. Besides, Agents, will get 50% (fifty per cent) commission on the net profits of the Worsted Plant. The net profits will be ascertained after deducting all the manufacturing expenses, interest, insurance, depreciation and selling commission, etc. For allowing annual depreciation in the value of the machinery and buildings and interest on the value of machinery, buildings and commencing from the date on which manufacturing actually starts under this Agreement, a lump sum of Rs. 50,000 has been agreed to the deducted for determining the net profits or loss position. In case of net loss, if any, there will be a deduction of 50% (fifty per cent) of such loss from the Agent's Account.

Analysing the terms of this sub-clause it would appear that the agents have been able to secure most liberal and profitable terms. To begin with they were to get a commission at the rate of one and a quarter per cent on the net proceeds of sales of all goods. There can be no objection to this. Secondly, the agents will get 50% commission on the net profits of the worsted plant. The net profits would have to be ascertained after deducting all the manufacturing costs, interest, insurance etc. The conduct of the agents in sharing half of the net profits does not appear to us to be consistent with the payments made to the agents for services rendered. It is difficult to lay down any rule of universal application as to what percentage of profit would be consistent with the payment in lieu of services but taking the totality of the provisions of the agreement it seems to us that the percentage of profits and the manner in which it is to be determined is more consistent with the position of a partner than that of an agent. Finally the provision for sharing the loss incurred by the company and for a lump sum deduction of Rs. 50,000 is totally inconsistent with a contract of agency. Furthermore, sub-clause (iv) of Clause 7 provides as under :

(iv) The commission account will be maintained separately by the Agents and the commission will be payable to the Agents by the Company every six months. In the same way, the amount of Rs. 25,000 for six months as provided in sub-clause (i) above, will be paid to the Company every half-year within ten days. The profit and loss account of the Worsted Plant will be made every six months within ten days and the adjustments will be made accordingly by actual payments, as the case may be, within ten days.

The above sub-clause clearly provides for a separate commission account to be maintained by the agents and the commission to be paid every six months. Consequently the agents agreed to pay a sum of Rs. 25,000 for six months every half year within ten days. We might further mention here that the provision in the agreement regarding sharing of the loss is absolutely peculiar to this particular agreement and there is not a single authority, which has, in spite of such a provision, held that the transaction does not amount to a joint venture or a division of profits. The provision regarding the consent of the agents to the sales and the programme of manufacture is also pertinent in order to determine whether the transaction amounted to a joint venture in the garb of a contract of agency. It is well settled that the Court in order to construe an agreement has to look to the substance or the essence of it rather than to its form. A party cannot escape the consequences of law merely by describing an agreement in a particular form though in essence and in substance it may be a different transaction. In these circumstances, therefore, if we construe the agreement as a sort of a joint venture or a transaction like a partnership which has been given the form and appearance of a contract of agency, the law must have its course.

8. Our attention has been drawn by the learned Counsel for the Revenue to a decision in British Sugar Manufacturers Ltd. v. Harris (Inspector of Taxes ((1939) 7 ITR 101 : (1938) 1 All ER 149)), where Greene, M. R. clearly observed that where a person contributes to some sort of joint

adventure which ultimately results in division of profits, it could not be construed as a remuneration for services. In this connection, Greene, M. R. observed as follows :

It is not cash that passes in exchange for these profits, it is services; and the badge of such a contract is remuneration for services, and therefore the first thing that this remuneration would certainly not be is a share of profits purchased by the employee. * * * * * I can conceive of a case where a person contributes to some sort of joint adventure services, while others contribute perhaps capital, land, plant, and goods, arranging between themselves (it may be something short of a partnership) that nobody shall get anything until the pool of profits is ascertained, and then they shall divide it up between them in specified proportions. That, it seems to me would be a real agreement for division of profits, because there would be one profits fund only. There would not be two 'profit' funds to be ascertained for different purposes.

These observations seem to us to cover the of the instant case. Having regard to the terms and conditions of the agreement detailed and analysed above, there can be no doubt that the agents by contributing to the investments and by sharing the profits as also the losses have actually contributed to a joint venture and ultimate division of the profits with the principals and the agreement must be construed as an agreement for division of the profits in specified proportions as mentioned therein. It is true that in the aforesaid case on the facts found the Court held that the transaction did not amount to a joint venture but it was clearly pointed out in the judgment that there is a very thin line of distinction between a contract for payment of a share of profits simpliciter and a payment of remuneration which is deductible in truth from the profits divisible. We, therefore, find ourselves in a complete agreement with the observations made by Greene, M. R., which aptly apply to the facts of the present case on the basis of the various clauses of the agreement dated October 20, 1955.

9. The High Court, however, appears to have relied upon the decision in Dharamvir Dhir's case (supra). The facts of that case appear to be clearly distinguishable from those of the present case. What had happened in Dharamvir Dhir's case was that the assessee was an employee of the firm earning a particular salary. The employee entered into a coal raising contract with a coal company and as he did not have the necessary funds he persuaded a public charitable trust to advance to him sums upto Rs. 1 1/2 lakhs on payment of interest at 6 per cent and share 11/16ths of the profits of the business. The assessee agreed that the coal raising contract would be carried on in accordance with the policy settled between him and the trust and the trust could withdraw its money at any time. It is, therefore, clear that in the first place the agent, namely, the trust, agreed to finance the assessee by giving him a loan of Rs. 1 1/2 lakhs at 6 per cent interest. This was undoubtedly permissible. The trust was also to get 11/16th of the profits of the business. It was, however, not agreed between the parties that the profits would be ascertained after deducting the net expenses as mentioned in the agreement before us. It is true that the contract was to be carried on in accordance with the policy settled between the assessee and the trust but that did not give any veto power to the trust to torpedo the contract. In the instant case the agreement clearly provided for the consent of the agents not only at the beginning of the manufacture of the yarn by the plant to be installed by the assessee company but at every stage in the programme of manufacture. Even at the stage of the sale of the products the consent of the agents was necessary. In other words, the agents were given a complete controlling power so far as the manufacture and sale of the products of the assessee company were concerned. No such stipulation is to be found in Dharamvir Dhir's case. Finally, not only there was no provision in Dharamvir Dhir's case under which the trust was to share the losses but there was an express provision to the contrary, namely, that the trust was not liable for any loss. Thus the mere payment of interest at the rate of 6 per cent on the loan advanced to the assessee and a percentage in the profits of the business would be quite consistent with a remuneration in lieu of

services lent and would certainly quite consistent with a remuneration in lieu of services lent and would certainly amount to an expenditure incurred by the assessee wholly and exclusively for the purpose of the business which was conducted by the assessee. The same, however, cannot be said of the present case. It was on the peculiar facts of the Dharamvir Dhir's case that this court observed as follows :

On the facts proved in the present case the trust agreed to finance the business of the appellant on the terms set out in the agreement and there is nothing to show that he could have made any better arrangements or would not have lost the contract if he had failed to enter into the agreement, i.e. the agreement to pay the amounts in dispute. Therefore, in a commercial sense, the payments were an expenditure wholly and exclusively laid out for the purpose of the business.

It may be mentioned that this Court had considered the decision in the British Sugar Manufacturers Ltd.'s case (supra) and had approved of the same.

10. Great stress was laid by Counsel for the assessee company on the fact that this Court could not go behind the commercial expediency which had to be determined from the point of view of a businessman. Even so whatever be the commercial considerations, it is difficult to hold that the commercial expediency dictated the assessee company to allow itself to be completely overshadowed by its selling agents so as to pay them not only for the services rendered but also allow them to share profits, control the manufacture of the goods and the programme thereof and also to share the losses. The test of commercial expediency cannot be reduced in the shape of a ritualistic formula, nor can it be put in a watertight compartment so as to be confined in a straitjacket. The test merely means that the Court will place itself in the position of a businessman and find out whether the expenses incurred could be said to have been laid out for the purpose of the business or the transaction was merely a subterfuge for the purpose of sharing or dividing the profits ascertained in a particular manner. It seems to us that in ultimate analysis the matter would depend on the intention of the parties as spelt out from the terms of the agreement or the surrounding circumstances, the nature or character of the trade or venture, the purpose for which the expenses are incurred and the object which is sought to be achieved for incurring those expenses. If the expenses incurred amount to a profit of an enduring nature they may be treated as capital expenditure, whereas if the expenses merely serve to promote or increase the commercial activity they may amount to an expenditure which is incurred for the purpose of the business.

11. Reliance was also placed by Counsel for the assessee company on the decision in J. K. Woollen Manufacturers v. C.I.T., U.P. (AIR 1969 SC 609 : (1969) 1 SCR 525 : (1969) 72 ITR 612), where this Court observed as follows :

The question as to whether an amount claimed as expenditure was laid out or expended wholly or exclusively for the purpose of business, profession or vocation as required under Section 10(2)(xv) of the Income Tax Act has to be decided on the facts and in the light of the circumstances of each particular case.

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In our opinion, neither the High Court nor the Appellate Tribunal has applied the proper legal test in this case. As pointed out by this Court in C.I.T., Bombay v. Walchand and Co. Private Ltd.((1967) 65 ITR 381 : AIR 1967 SC 1435 : (1967) 3 SCR 214) in applying the test of commercial expediency for determining whether an expenditure was wholly and exclusively laid out for the

purpose of the business, reasonableness of the expenditure has to be adjudged from the point of view of the businessman and not of the Income Tax Department. It is, of course, open to the Appellate Tribunal to come to a conclusion either that the alleged payment is not real or that it is not incurred by the assessee in the character of trader or it is not laid out wholly and exclusively for the purpose of the business of the assessee and to disallow it. But it is not the function of the tribunal to determine the remuneration which in their view should be paid to an employee of the assessee.

It would appear that in the aforesaid case the only question was regarding the quantum of remuneration to be given to the General Manger and this Court observed that the businessman must be given complete freedom to fix the terms of his employees after taking an overall view of the situation. This was not at all a case where an agreement like the present one was entered into between the assessee company and its agents. On the other hand in C.I.T., Kerala v. Travancore Sugars and Chemicals Ltd. ((1973) 88 ITR 1, 10 : (1973) 3 SCC 274 : 1973 SCC (Tax) 186) this Court added a word of caution that the test of commercial expediency should not be applied in a mechanical manner and observed as follows : [SCC p. 281 : SCC (TAX) p. 193, para 15]

In considering the nature of the expenditure incurred in the discharge of an obligation under a contract or a statute or a decree or some similar binding covenant, one must avoid being caught in the maze of judicial decisions rendered on different facts and which always present distinguishing features for a comparison with the facts and circumstances of the case in hand. Nor would it be conducive for clarity or for reaching a logical result if we were to concentrate on the facts of the decided cases with a view to match the colour of that case with that of the case which requires determination. The surer way of arriving at a just conclusion would be to first ascertain by reference to the document under which the obligation for incurring the expenditure is created and thereafter to apply the principle embalmed in the decisions of those facts. Judicial statements on the facts of a particular case can never assist courts in the construction of an agreement or a statute which was not considered in those judgments or to ascertain what the intention of the legislature was. What we must look at is the contract or the statute or the decree, in relation to its terms, the obligation imposed and the purpose for which the transaction was entered into.

The learned Counsel for the assessee company relied on the aforesaid case because the question whether the transaction amounted to a joint venture appears to have been raised but it appears that this point had been given up when the case was sent on remand and was therefore not decided. In these circumstances, the decision in the aforesaid case does not appear to be of any assistance to the assessee company.

12. The tribunal had interpreted the agreement keeping into account the tests of commercial expediency and we find ourselves in complete agreement with the view taken by the tribunal. The High Court on the other hand relied upon what it called the surrounding circumstances that the assessee company was a losing concern from its inception and had to get rid of the previous selling agents M/s. Murlidhar Chiranjilal because they caused considerable embarrassment to the assessee company. While the standing Counsel for the Revenue has admitted that the company was running at some loss there was no evidence that the company was in such a bad shape that it had to get rid of the first selling agents because the selling agents were causing embarrassment to it. The High Court then relied on the fact that the first agency which was entered into with M/s. Murlidhar Chiranjilal in 1953 also resulted in loss as a result of which the second agreement dated October 20, 1955 was entered into. This does not appear to be of much consequence. The High Court then relied on the fact that the agents had no other connection with the assessee company except that of the business connection. The High Court further found that the promoter of the assessee company Mr. Desh

Bandhu Gupta had a stature which enabled him to borrow loans from the banks on personal security and as he died in an air crash the credit of the company went down and it was not able to raise money from the banks. There is absolutely no warrant for these facts referred to by the High Court which are neither mentioned in the agreed statement of the case submitted by the tribunal to the High Court nor in the order of the tribunal. It is well settled that the High Court is not entitled to go behind the statement of the case. In C.I.T., Poona v. Manna Ramji and Company (86 ITR 29,37 : (1973) 3 SCC 43 : 1973 SCC (Tax) 93) this Court observed as follows : [SCC p. 49 : SCC (Tax) p. 99. para 11]

In this respect we are of the view that the tribunal is the final fact-finding authority. It is for the tribunal to find facts and it is for the High Court and this court to lay down the law applicable to the facts found. Neither the High Court nor this Court has jurisdiction to go behind or to question the statement of facts made by the tribunal. The statement of case is binding on the parties and they are not entitled to go behind the facts of the tribunal in the statement. When the question referred to the High Court speaks of "on the facts and circumstances of the case", it means on the facts and circumstances found by the tribunal and not on the facts and circumstances as may be found by the High court.

13. In C.I.T., Bombay v. Poona electric Supply Co. Ltd. ((1963) 49 ITR 913, 924 (Bom)), the Bombay High Court observed as follows :

It is true that the electricity Act exercises control on the business of the licensee, but the control that is exercised by reason of the aforesaid proviso is to compel the assessee to distribute part of its clear profits if it is found that "clear profits" are in excess of the reasonable return as contemplated under the Act. That, in our opinion, would only amount to apportionment or distribution of the profits after they have been earned. It cannot, therefore, be said that the amount set apart for the purpose of distribution amongst the consumers is not chargeable to tax on the ground that it represents overcharge.

This case however was decided on its own facts and has no application to the facts in the instant case.

14. Reliance was also placed by Counsel for the assessee company on a Division Bench decision of the Patna High Court in Jamshedpur Motor Accessories Stores v. C. I. T., Bihar & Orissa ((1974) 95 ITR 664, 672 (Pat) where Untwalia, C. J., as he then was, observed as follows :

That position being accepted the matter as to what amount was payable to Parikh ought to have been adjudged from the assessee's point of view and not from the department or tribunal's point of view. It has to be emphasised that unless there is a limitation put by the law on the amount of expenditure a lesser amount than the amount expended cannot be allowed merely because the assessing authority thinks that the assessee could have managed by paying a lesser amount as a prudent businessman. The test of prudence by substituting its own view in place of the businessman's has not been approved by the Supreme Court in the decision referred to above.

Here also the observations were confined only to the question that the test of prudence was to be determined from the point of view of the businessman Jamshedpur Motor Accessories Stores case was also concerned regarding the quantum of the payment of commission and does not appear to be useful in deciding the point at issue in the present case.

15. Some other decisions were cited at the Bar but they have no bearing on the issue and it is not necessary for us to refer to them. What is, therefore, important to us is that no decision has been cited before us which takes the view that even though under the contract of agency the selling agents who agreed to make substantial investments in the assessee company and got interest on the loans apart from the commission they also shared profits to the extent of 50% as also loss to that extent and had complete controlling power in the manufacturing programme or the sale of the products and yet the transaction would be one of agency simpliciter and not a joint venture. On the facts found by the tribunal and those mentioned in the statement of the case as discussed above leads to the inescapable conclusion that the present contract of agency really amounts to a transaction by which substantial investments had been made by the selling agents with a view to control the manufacturing programme and the agents had also agreed to share the profits and losses equally. This is, therefore, nothing but a joint venture to divide the profits after the same are ascertained and cannot in any sense be deemed to be expenses incurred by the assessee company for the purpose of its business or for that matter for earning profits. In fact in Pondicherry Railway Co. Ltd. v. C. I. T., Madras (AIR 1931 PC 165, 170 : 58 IA 239), Lord Macmillan pointed out that a payment out of profits and conditional on profits being earned cannot be legitimately described as a payment made to earn profits. It assumes that profits have first come into existence. But profits on their coming into existence attract tax at that point and the Revenue is not concerned with the subsequent application of the profits. In this connection the Privy Council observed as follows :

It is claimed for the company that when it makes over to the Colonial Government their half of the net profits it is making an expenditure incurred solely for the purpose of earning its own profits. The court below has unanimously negatived this contention and in their Lordships' opinion has rightly done so. A payment out of profits and conditional on profits being earned cannot accurately be described as a payment made to earn profits. It assumes that profits have first come into existence. But profits on their coming into existence attract tax at that point and the Revenue is not concerned with the subsequent application of the profits. * * * * * * *

But the principle laid down by Lord Chancellor Halsbury in Gresham Life Assurance Society v. Styles (1892 AC 309, 315 : 62 LJQB 41 : 67 LT 479) is of general application unaffected by the specialities of the English tax system :

..... But when once an individual or a company has in that proper sense ascertained what are the profits of his business or his trade, the destination of those profits or the charge which has been made on those profits by previous agreement or otherwise is perfectly immaterial. The tax is payable upon the profits realised and the meaning to may mind is rendered plain by the words "payable out of profits".

16. Thus in short by controlling the manufacturing programme, sharing to the extent of 50% in the net profits ascertained in the manner stipulated in the agreement and above all for sharing 50% of the losses which are to be deducted from the commission of the agents the agents become completely equated with the proprietors of the firm itself and therefore the contract of agency is really a sort of a partnership and has been given the cloak and colour of a agency to conceal the real intent and purpose of the commercial venture.

17. In view of the decisions referred to above and the peculiar facts of the present case we are satisfied that the view taken by the tribunal that the payments in question were not legally deductible under Section 10(2)(xv) of the Act was correct. The view taken by the High Court that the amounts in question were deductible under Section 10(2)(xv) appears to be legally erroneous

and cannot be upheld.

18. For the reasons given above, the appeals are allowed and the judgment of the High Court is set aside and that of the tribunal is restored and the two questions referred to the High Court are answered against the assessee company and in favour of the Revenue. In view of the peculiar facts of the present case, we leave the parties to bear their own costs in this Court.

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