

BOMBAY HIGH COURT

R.B. Bansilal Abirchand Spinning

Vs

Commissioner of Income-Tax

(D Padhye, C.J. N Abhyankar, J.)

17.03.1969

JUDGMENT

Abhyankar, J.

1. This judgment will govern the references in all these cases. In all these references, there is one common question referred. In addition, there is a second question referred in Income-tax Reference No. 66/63 and a third question which is referred in Income-tax Reference No. 6/66. We propose to answer two out of these three questions in this common judgment. The facts giving rise to these questions are, more or less, common as the assessee is the same. The relevant statement of facts in respect of each of these questions will be reproduced at the appropriate stage.

2. In respect of the question which is common in all the cases, the order of reference under section 66(2) of the Indian Income-tax Act and the statement of the case are as follows :

"We are required by the High Court of Judicature at Bombay by its order under section 66(2) of the Indian Income-tax Act, dated 7th July 1959, in I. T. Application No. 54 of 1957, to refer to it the following question arising out of the order of the Tribunal in I. T. A. Nos. 3856 and 3857 and E. P. T. A. Nos. 983 and 984 of 1948-49 'Whether, in the circumstances of this case, the Tribunal or other income-tax authorities were precluded in law from going behind the agreement of purchase dated the fourteenth day of October one thousand nine hundred and forty-five in order to ascertain the original cost of the plant, machinery and buildings to the applicant by reason of the fact that such cost had been specifically set out under separate heads in the schedule to the said agreement and also the fact that the mill and other buildings were valued by Mr. Vaze and the plant and machinery were valued by Mr. Belcham prior to the date of the said agreement as stated in their respective reports dated the tenth day of April one thousand nine hundred and forty-five and the twentieth day of March one thousand nine hundred and forty-five ?'

3. The assessee is a registered firm owning a textile mill in Hinganghat. The assessment years for the purpose of income-tax are 1946-47 and 1947-48 and the corresponding previous years are Diwali years ending on November 4, 1945, and October 24, 1964, respectively. The excess profits tax assessments under reference relate to the chargeable accounting periods ending on November 4, 1945, and March 31, 1946, respectively. The excess profits tax assessments are merely consequential and the answer of the hon'ble court to the question will determine not only the income-tax assessments but also the excess profits tax assessments.

4. A firm in the name of R. B. Bansilal Abirchand, consisting of four partners, namely, (1) Raja Sir Bisesardas Daga, (2) Seth Narsingdas Daga, (3) Seth Badridas Daga and (4) Seth Ramnath Daga, owned the textile mill at Hinganghat and the agency shop attached to it. That firm was dissolved on or about October 20, 1939, and the assets of that firm, namely, the textile mill and the agency shop, were purchased for a consideration of Rs. 26,11,042 by Seth Narsingdas Daga and Seth Ramnath Daga, who constituted a new firm. The new firm also was dissolved on October 18, 1944, and the mill and the agency shop were purchased by Seth Narsingdas Daga for Rs. 50,00,000 upon terms and conditions contained in an agreement of purchase dated 14th October, 1945. The purchase was given effect to from October 18, 1944, i.e., the date of the dissolution of the firm. The schedule to that agreement showed details of the valuation of the various assets purchased and the value of the plant and machinery was fixed at Rs. 21,00,000 and the mill building at Rs. 6,32,650. The building was valued by one Mr. Vaze, an architect, and the plant and machinery were valued by one Mr. Belcham, former manager of the mill. On the same day i.e., on the date of the agreement, the family of Seta Narsingdas Daga was disrupted and the mill and the agency shop were taken over by the assessee firm consisting of seven partners, namely, (1) Smt. Sodradevi Daga, (2) Seth Dwarkadas Daga, (3) Seth Vithaldas Daga, (4) Jamnadas Daga, (5) Seth Goverdhandas Daga, (6) Seth Hiralal Daga and (7) Seth Sunderlal Daga. The partnership agreement was executed on October 24, 1945, but the firm was constituted as from 18th October, 1944, for a period of five years. The agreement of purchase dated October 14, 1945, along with the schedule, is made a part of the case and is marked annexure "A". The valuation reports of M/s. Vaze and Belcham are marked annexures "A-1" and "A-2" respectively, and form part of the case. The partnership deed dated October 24, 1945, is made a part of the case and is marked annexure "B".

5. The assessee-firm claimed before the Income-tax Officer that it should be given depreciation on machinery and building on the basis of their original cost as determined in the schedule to the agreement referred to in the earlier paragraph. For the assessment year 1946-47, the Income-tax Officer rejected the claim of the assessee and fixed the value of the buildings at Rs. 5,30,000 and of the textile machinery at Rs. 15,10,000. His order for the year 1946-47 is made a part of the case and is marked annexure "C". For the assessment year 1947-48, he has followed the same

basis for determining the depreciation on machinery and buildings and his order for the year 1947-48 is not made a part of the case because there is no discussion in that order on the point in dispute in this reference.

6. The assessee appealed to the Appellate Assistant Commissioner, who confirmed the decision of the Income-tax Officer, although through mistake he has taken the value of the machinery to be Rs. 15,00,000 instead of Rs. 15,10,000. His order for the year 1946-47 is made a part of the case and is marked annexure "D". For the assessment year 1947-48 also he confirmed the decision of the Income-tax Officer, but since he has not discussed in detail the point at issue in this reference, his order for the year 1947-48 is not made a part of the case.

7. The assessee thereafter appealed to the Tribunal and, by its order dated November 4, 1949, it remanded the case back to the Income-tax Officer for further enquiry relating to the claim of depreciation allowance on machinery and buildings. The Income-tax Officer thereafter submitted his report in which he maintained that the valuation of buildings including land was Rs. 5,00,000 out of which, valuation of land was Rs. 30,000 and that the valuations of machinery and plant could only be Rs. 6,19,650. He arrived at these valuations on the assumption that the goodwill of the business was Rs. 16,00,000 and the agreement had not made adequate allowance for the goodwill because, according to the agreement, goodwill and trade marks were valued at only Rs. 10,000. The Tribunal, after considering the remand report of the Income-tax Officer, confirmed the orders of the income-tax authorities for reasons given in paragraph 3 of its order. The Tribunal's remand order, the Income-tax Officer's remand report and the Tribunal's final order are made parts of the case and are marked annexures "E", "F" and "G", respectively.

8. This case is stated as required by the hon'ble court by reference to the question of law as stated in paragraph 1 above. The statement is agreed to by the parties."

9. It will be seen from the facts mentioned in the statement of the case itself that the assessee is a partnership which has been registered under section 26A of the Indian Income-tax Act, 1922, and comprises of members of the erstwhile Hindu undivided family excluding Rai Bahadur Seth Narsingdas Daga. The deed of dissolution of partnership, which is annexure "A" attached to the statement of the case, recites that the parties to the previous partnership, which had come into existence on 21st day of October, 1939, carried on the business of the spinning and weaving mill at Hinganghat in the name and style of "Rai Bahadur Bansilal Abirchand Spinning and Weaving Mills" and the said partnership was dissolved, by mutual consent, on 18th October, 1944. It also recites that, as a part of the agreement to dissolve the partnership, it was also agreed between the two partners that the said two business including the goodwill, trade marks, etc., connected therewith will be purchased from the partnership along with the assets by one of the partners, namely, Seth Narsingdas Daga. After the dissolution and acquisition of the partnership assets

along with the two business, by the family of Seth Narsingdas Daga, there was a simultaneous disruption of the said Hindu undivided family of Seth Narsingdas Daga and the business acquired was decided to be carried on by a new partnership consisting of members of the disrupted family of Seth Narsingdas Daga excluding Narsingdas Daga himself. The actual agreement of purchase of the assets, etc., however, was incorporated in a document dated 14th October, 1945, and, according to the recites of this deed, the total price that was payable by the purchaser was fixed at Rs. 50,00,000. The break up of Rs. 50,00,000 is shown in annexure "A", that is, the agreement of purchase, in full details. The property comprised of immovable property such as bungalows, building at Nagpur and Hinganghat, agents' quarters and other adjoining houses in Hinganghat, gardens and malguzari share of mouza Hinganghat, other movable assets which were rolling stock, utensils, materials, furniture, cotton, cotton-seeds, etc., enumerated in great detail in the schedule. It also comprised the cost of the mill-plant including gin and press factories which were shown as valued at Rs. 21,00,000 for the machinery and Rs. 6,32,650 for the mill's buildings.

10. For the assessment year 1946-47 corresponding to the account period ending Diwali of 1945, the assessee-firm claimed that the cost of mill-plant lands and buildings pertaining to the mill as shown in the mill books at Rs. 21,00,000 and Rs. 6,32,650 should be taken as the cost at which the depreciation should be claimed. The main contention of the parties in this and the subsequent year is as the proper valuation of these two depreciation assets. The Income-tax Officer did not accept this valuation. He observed that he had looked into other factors such as the fire insurance policies effected by the assessee near about the year transfer and had also considered cases of transfers of mills. He also kept in view the fact that the mill was formerly partially owned by the family of R. B. Seth Narsingdas Daga and that there was considerable rise in the prices of spinning and weaving machinery. All considered, however, he fixed the value of the depreciable assets of the assessee at Rs. 5,00,000 for the buildings of the mills, etc., instead of Rs. 6,32,650 claimed by the assessee and the value of machinery at Rs. 15,10,000 instead of Rs. 21,00,000 as claimed by the assessee. By way of a further explanation of his valuation, the Income-tax Officer observed that as Seth Ramnath Daga owned half share, the assessee should have paid the entire amount of consideration falling to his share immediately on acquiring the assets. Being short of funds the assessee did not make the payment all at once and substantial amount of interest had to be paid to Seth Ramnath Daga. Evidently the major portion of the payments to be made pertained to the value of fixed assets and as such part of the interest payment to Seth Ramnath Daga must be considered to be towards payment of those assets. Therefore, out of the total interest payable and which had to be paid to Ramnath Daga, he capitalised a sum of Rs. 8,000 as forming part of the capitalised value of the assets.

11. When the matter went before the Appellate Assistant Commissioner, so far as the Income-tax

Officer had disallowed a part of the interest paid to Seth Ramnath Daga, the assessee's contention was accepted and deduction of Rs. 8,000 out of the interest paid was deleted. With regard to the valuation of the depreciable assets, the Appellate Assistant Commissioner has dealt with it as ground No. 7. The appellate authority has pointed out that the Hindu undivided family of R. B. Narsingdas Daga also disrupted on that date on which there was a dissolution of the firm of Seth Narsingdas Daga and Ramnath Daga and the ownership of the concern vested in a firm which consisted of all the members of the family except R. B. Narsingdas Daga. The Appellate Assistant Commissioner also observed that it was a fact that the firm of the two partners was dissolved on Diwali of 1944 and the running concern was taken over by the other partner. The price was fixed after mutual agreement and after taking into consideration the market conditions. The Appellate Assistant Commissioner also accepted that the assessee was entitled to claim depreciation on the original cost, that is, the price paid by him to the other party, and not on the written down value as appearing in the account books of the predecessor. In paragraph 9 of his order, the Appellate Assistant Commissioner observed that it was clear that the transaction was settled for a sum of Rs. 50,00,000 as against Rs. 27,00,000 determined in 1939, when the original partnership was dissolved and a new partnership of Narsingdas and Ramnath Daga was formed. He also observed that the trade conditions had materially changed. The market rates prevailing on Diwali 1945 should be taken as a guidance in fixing the original cost of machinery and buildings to the assessee. He has also observed that, due to keen demand and less supply, prices of even second-hand machinery had soared very high and the market had shown an upward tendency, and that the prices reached the climax during these years due to restrictions on imports. But the learned Appellate Assistant Commissioner felt that inasmuch as Seth Narsingdas was already a partner in the concern and he had vested interest to the extent of 8 annas, he was not expected to purchase the property which belonged to himself. He was not out of pocket to this extent and, even assuming, without admitting, that the consideration paid was adequate to Seth Ramnath Daga, he was not entitled to deduct depreciation on the machinery and buildings at an inflated figure in his own case as he was the owner of half of the machinery and buildings purchased by him. He could not purchase the eight annas share which already belonged to him and keeping this fact in view he entirely agreed with the views expressed by the Income-tax Officer and felt that the Income-tax Officer had not gone wrong in determining the original cost of the machinery and the buildings at Rs. 15,00,000 and Rs. 5,00,000, respectively. It is an admitted position that the reference to Rs. 15,00,000 is not correct and the correct figure is Rs. 15,10,000 as the price determined for the depreciable machinery, etc.

12. In a further appeal to the Tribunal at the instance of the assessee at the initial stage the Tribunal felt that the valuation of the goodwill and the valuation of the land and mill building, etc., required to be further probed and therefore remanded the matter to the Income-tax Officer for a fresh report. Such a remand report was submitted by the Income-tax Officer estimated the

price of the goodwill at Rs. 16,00,000 of the machinery and plant at Rs. 6,19,650 and of the buildings at Rs. 4,70,000 plus Rs. 30,000. On receipt of this report, it does not appear that the Income-tax Appellate Tribunal was much impressed by the findings of the Income-tax Officer on remand. With regard to the remand report, the Appellate Tribunal in its final order observed that they did not consider necessary to decide whether the value given by the Income-tax Officer to goodwill in his remand report is proper. They only observed that the valuation of Rs. 10,000 given by the assessee was low. Ultimately the Appellate Tribunal confirmed the valuation made by the Appellate Assistant Commissioner. With regard to the report regarding the valuation of the machinery made by the consulting engineer, Mr. Belcham, the Tribunal observed that Mr. Belcham may be a good manager of the mill, but a proper person to give evidence in regard to the value of the Machinery would be a dealer in machinery and also pointed out that Mr. Belcham's valuation was in round figures. It further observed that prices of machinery had gone up considerably in 1945, on account of the war, but they were not prepared to believe that machinery and plant was worth Rs. 21,00,000 in October, 1945, and that the written down value in 1939 was a little less than Rs. 21,00,000. As regards the report of the engineer, Mr. Vaze, regarding the valuation of the building of the mill, the Tribunal observed that, however competent a consulting engineer may be, if he wants to satisfy the court about the valuation made by him of a property, he should base the valuation not on an appraisalment but on detailed measurements and this has not been done. Ultimately, the Tribunal observed as follows :

"In our opinion, the valuation made by the Income-tax Officer in his assessment order are reasonable and we accept them as the actual cost to the assessee....."

13. Thereafter the assessee desired by an application under section 66(1) of the Indian Income-tax Act, 1922, the Tribunal to make a reference to the High Court in respect of the question of valuation of the depreciable assets of the machinery and the buildings, but the Tribunal declined to do so. The assessee made a further application to this court and this court required the Tribunal to refer the question which is reproduced above, and it is, in these circumstances, as required by this court, that the Income-tax Appellate Tribunal has made the reference along with the statement of the case.

14. In support of this reference it is contended that it is not disputed that in fact a sum of Rs. 50,00,000 has been paid by the assessee with respect to all assets and the two businesses. According to the learned counsel for the assessee what was decided in October, 1944, was that the previous partnership should be dissolved and that one of them, that is, R. B. Narsingdas Daga, should acquire the assets and the two businesses along with all the property comprising the two businesses. The time of dissolution being the end of the Diwali year, it was not possible to accurately or definitely calculate either the quantum of the price of the different articles because

the mill was in the midst of production and considerable time was required to be taken to make detailed calculations of different assets and properties. With regard to the schedule which forms part of the agreement of purchase it is stated that the stocks of machine, yarn, cloth, cotton-seeds, other materials, rolling stocks, etc., had to be inventoried. These details had naturally involved considerable time. They had employed services of two independent experts, one for valuation of the buildings and another for valuation of the machinery and it was on the basis of the valuation made by these experts that the final amount and valuation of different parts of the machinery, buildings, structures and other materials was valued and determined between the parties. It has naturally taken time and the actual valuation report in respect of the building was made by Mr. Vaze, dated 10th April, 1945, and the valuation regarding the machinery was made by Mr. Belcham on 20th March, 1945. It was after receipt of these detailed reports that the final agreement was possible. If it is not disputed, as it does not appear to be disputed, that the purchaser in fact actually paid a sum of Rs. 50,00,000 though half of the price represented the share of the purchasing partner himself, it was not possible without any finding to that effect for the departmental authorities to look with suspicion in respect of the price of the machinery and the buildings of the mills for the purpose of determining their value or cost to the assessee. The criticism about Mr. Vaze's report that he has not based his calculations on measurements is not correct because in the report, annexure "A-1", Mr. Vaze has expressly stated in the opening paragraph that he had taken the necessary measurements with a view to ascertain the present value and has also taken into account the age of the buildings, their situations, constructions, their present conditions and use and after carefully finding out the different consistent and appropriate scale of rates regarding different structures, such as on the plinth area basis, he has worked out the values. As regards Mr. Belcham, though he was a retired engineer on the day he submitted his valuation report, he was employed in the mills at one time as chief engineer in charge of the machinery and was a competent person to make a valuation of the machinery in its different parts and submit a report. It is urged that there was no circumstance in this case which could justify the Tribunal or the income-tax authorities going behind the agreement of the purchase which gave in sufficient details the price at which the machinery and building were separately valued and paid for. The learned counsel for the assessee has urged that it is not his case that there is any legal bar precluding the authorities from going behind the agreement of purchase in a given case. The contention of the assessee is that, in the circumstances of this case, however, the authorities were precluded from going behind the agreement as there was no allegation of any suppression or any deceit or any fraudulent making of accounts which would justify the valuation made in the agreement to be looked with suspicion.

15. In this connection, reliance was placed on a recent decision of the Supreme Court in *Kalooram Govindram v. Commissioner of Income-tax*. That was a case where in a suit for partition between two members of a Hindu undivided family each was declared entitled to a

particular share and each item of property which could not be divided by metes and bounds was put up for sale by competitive bidding between them. One of the items was a sugar factory which was knocked down in favour of one on the members who had 10/16th share for Rs. 34,00,000. After all the items of the properties were thus allotted to one or the other of them, final adjustment was made by cash payment. The question arose whether G who had purchased the factory at Rs. 34,00,000 was entitled to depreciation on the factory under section 10(2) (vi) of the Indian Income-tax Act, 1922, on the amount of Rs. 34,00,000 depreciation not having been allowed for an earlier period. The Appellate Tribunal held that, as regards the 10/16th share of the purchaser, the cost to the appellant was the original cost to the larger family, and, as regards the 6/16th share, the original cost was 6/16 of the purchase price of Rs. 34,00,000, namely, Rs. 12,75,000. On a reference at the instance of the assessee, the High Court held that depreciation ought to be computed on the basis of the original cost to the larger family and not on the basis of the valuation on which the appellant took over the assets. On appeal before the Supreme Court, the majority view was that division by metes and bounds, whether it involves transfer or not within the meaning of the Transfer of Property Act, does confer on a divided member an absolute title to a specified property and barring the cases of fraud, collusion and inflation and deflation of values for ulterior purposes, the cost of an asset to a divided member must necessarily be its cost to him at the time of partition, whether mentioned in the partition deed or ascertained aliunde. If the valuation of the property for purposes of partition was not nominal but was real and that was the basis for allocating properties to different members, the cost of a property allotted to a member cannot be that at which it was purchased by the joint family in the remote past, but would be the value given to it for the purpose of allotment or at which it was auctioned for the purpose of partition. Relying on this decision, it is urged that the cost of different materials and cost of property which was purchased by one of the partner is the cost actually paid and Rs. 50,00,000 is not a notional cost in respect of the items, but actual cost arrived at after due valuation, calculation and enumeration. As there is no allegation of any fraud or deliberate deflation or inflation, nor any finding to that effect by any of the authorities, it is contended that this is not a case in which the authorities could be justified in going behind the agreement of purchase.

16. As against this contention, it is urged on behalf of the revenue that the recitals in the agreement of purchase to the following effect, namely :

"AND WHEREAS the parties hereto were entitled to the profits and liable for the losses of the said business in equal shares and whereas the said partnership was dissolved by mutual consent on Kartak Sud, 1, S. Y. 2001 (18th October, 1944), Rai Bahadur Narsingdas agreed to purchase from the said partnership the assets and effects of the said two businesses including the goodwill thereof and the trade marks connected therewith at

the prices of the different assets of the said two businesses mentioned in the schedule hereunder written amounting to a total of Rs. 50,00,000 (rupees fifty lakhs)....."

17. are misleading and do not accurately represent the state of affairs as they must be on the date of dissolution and agreement of purchase by the partner. It is urged that, admittedly, the valuation of different parts as per the schedule of this agreement was arrived at at a much latter period and, in respect of the disputed items, only after obtaining the reports of valuation from Mr. Vaze and Mr. Belcham and the attempt seems to be to fit in the valuation with total price of Rs. 50,00,000 which must have been agreed between the parties at the time of the agreement of purchase. If it were possible for us to accept this interpretation of the agreement in annexure "A" there could be something in favour of the view taken by the department; but we are unable to hold that on the date of dissolution and at the time when it was agreed that the assets and the businesses should be purchased as going concerns by one of the partner, there was any agreement to purchase them at Rs. 50,00,000. There is no evidence to that effect before us, or on the record of the case. On the other hand, the interpretation put on the agreement by the learned counsel appearing for the assessee seems more reasonable and probable. According to the assessee what was agreed at the time of the dissolution of the previous partnership and purchase of the assets and the businesses as going concerns, was an agreement to the effect that Seth Narsingdas Daga should purchase the property at a price to be fixed after proper calculation and valuation. At that stage, that is on the date of the dissolution and agreement of purchase on 18th October, 1944, it was not possible for the contracting parties to know definitely what would be the reasonable valuation or price of different assets. That valuation was agreed to be arrived at by an independent assessment and for which purpose reports were called for from the experts, such as the building engineer, Mr. Vaze, and the chief engineer of the mill, Mr. Belcham. The valuation of the other properties and materials, that is, rolling stock, cotton, cotton-seeds, yarns, stock of cloth, etc., was also to be made which was bound to take considerable time as it did and it was only after calculating the value or prices of these different assets that ultimately the price was fixed at Rs. 50,00,000. The suggestion, therefore, that the valuation of the depreciable machinery and the buildings at Rs. 27,32,650, even though the price of Rs. 50,00,000 was already agreed, does not appear to be well founded. It is true that the valuation made by the chief engineer is in round figures, but on that account we are unable to hold that it was liable to be rejected. There is no other material on record to show that the valuation which has been made by Mr. Belcham either was exaggerated or incorrect. The Income-tax Officer has referred to the written down value but that has no relevance in determining what the cost of the assets it to a purchaser. That cost has to be ascertained by what price could reasonably be paid taking into account the conditions of the market. It seems to be as admitted position that, even though the machinery was old, on account of the dearth of the textile machinery and the fillip given to the textile trade and production on account of conditions created by war and non-availability of new textile machinery or even old

textile machinery, the price that was paid had to be compared according to the market conditions then prevailing. The position of the market has been referred to in the orders of all the three authorities in the department. We also do not find any basis for rejecting or under-estimating the report of Mr. Vaze regarding the valuation of the buildings made by him. The Tribunal has remarked that Mr. Vaze's report did not give details. That does not appear to be correct because the report itself states that the measurements were taken and valuations has been made after advertence to the plinth area of the structures, scale of rates, situations, and constructions and the present conditions of the buildings being taken into account.

18. In this connection, a reference was made to a decision in Jogta Coal Co. Ltd. v. Commissioner of Income-tax, on behalf of the department. The case related to the purchase of a lease-hold interest in a coal mine and it was found that the appellant-assessee had failed to produce any evidence in support of the market price of any of the items of plant and machinery and the calculation of coal was found to be inordinately low. On a parity of reasoning it is suggested that in this case also calculation of goodwill at Rs. 10,000 in respect of a textile mill and two businesses purchased for Rs. 50,00,000 is unduly low and has been deflated in order to keep a margin for inflating the value of the depreciable assets. The valuation of goodwill and trade marks at Rs. 10,000 is explained on behalf of the assessee by pointing out that those were the days of the complete control on textile production and that very little turned on either the trade mark or the goodwill of a particular producer, there being an acute shortage and scarcity of textile goods. Under the provisions of the Textile Control Order then in operation, at every stage there was a check on production and distribution and the manufacturers were not free agents to sell the goods once they were manufactured, but the goods had to be sold to designated purchasers under the orders of the authorities. In this state of the market, the goodwill was of little consequence and, therefore, the value put on the goodwill cannot said to be deliberately deflated. In our opinion, the mere fact that the goodwill was valued at Rs. 10,000, even assuming it may somewhat low, is not indicative of an inference that valuation of the depreciable assets such as the machinery and the buildings of the mill was deliberately exaggerated. If there is no such material, and we have not been shown any, in our opinion, the assessee was entitled to say that the authorities could not, in law, go behind the agreement in the absence of certain material. It is not the contention of the assessee, and we do not understand it to mean, that in no case the income-tax authorities are able to go behind the agreement of purchase. As pointed out in the decision of the Supreme Court, if there is material to show that there has been fraud, collusion, inflation or false transaction made with ulterior purpose, the cost of the asset as reflected in the agreement to purchase is not binding on the authorities, but, in the absence of any such circumstance, in view of the acts of this case, in our opinion, it must be held that in this case the Tribunal and the authorities were precluded from going behind the agreement in determining the purchase price. We do not find any basis for determining the valuation of the machinery at Rs.

15,10,000 instead of Rs. 21,00,000 made by the expert or the value of the building at Rs. 5,00,000 instead of Rs. 6,32,650 as estimated by the building engineer. Such an action introduces an element of arbitrariness and we do not think that, in the circumstances of this case, the Tribunal or the income-tax authorities could have gone behind the agreement of purchase, it not having been disputed that, in the light of the agreement, the purchaser had paid that must amount which was the cost of the purchase to him.

19. After having carefully considered the material on record and the submissions made on either side, we have come to the conclusion that the answer to the common question referred to us in all these references must be in the affirmative and in favour of the assessee. We accordingly answer the question No. 1 to the effect that, in the circumstances of this case, the Tribunal or the income-tax authorities were precluded, in law, from going behind the agreement of purchase dated 14th October, 1945, in order to ascertain the original cost of the plant, machinery and buildings to the assessee be reason of the fact that such cost had been specifically set out under separate heads in the schedule to the said agreement and also the fact that the mill and other buildings were valued by Mr. Vaze and the plant and machinery were valued by Mr. Belcham prior to the date of the said agreement as stated in their respective reports.

20. It is common ground that the consequential calculation of tax or the profit tax in all the subsequent years will be affected primarily by the answer to the first question which is common in all these references. In view of this answer, the other references in which such question does not (sic) arise will be disposed of accordingly.

21. This takes us to the second question which arises only in Income-tax Reference No. 66 of 1963. The reference is again at the instance of this court being required to be made by the Income-tax Appellate Tribunal. The question is as follows :

"Whether there are any materials on the record on which a sum of Rs. 50,000 (rupees fifty thousand) was included in the total income of the applicant on account of the alleged understated production of yarn and soft waste ?"

22. The relevant statement of the case is reproduced from paragraph 8 of the reference order up to paragraph 11 and is as follows :

"The second question is confined only to the assessment year 1949-50. The quantitative analysis of the working of the spinning department of the mill for the year concerned showed that on consumption of cotton weighing 35,22,080 lbs. yarn the soft waste produced was only 31,54,786 lbs. showing a dead loss of about 10.6 per cent. In the immediately preceding year, on consumption of 37,45,208 lbs. the percentage was only

7.9 Moreover, the loss of weight in the spinning department is mainly in the blow-room and the shortage in the blow-room for the year in dispute was only 6.03 per cent. as against 8.67 per cent. in the preceding year. The assessee had not maintained separate registers for sections other than the blow-room and its explanation for the excessive shortage was that the cotton of inferior variety had been mixed and was responsible for increased shortage and it relied on the technological report on the trade varieties of the Indian Cotton, 1949, published by the Indian Central Cotton Committee. The Income-tax Officer did not accept this explanation and added an amount of Rs. 1 lakh to cover for unaccounted production on yarn and soft waste. His order is made a part of the case and is marked annexure 'H'.

23. The assessee-firm thereupon appealed to the Appellate Assistant Commissioner and contended that it was physically impossible to maintain registers regarding quantities for processes after cotton leaves the blow-room, that shortage in the blow-room is determined by factors which may adversely affect the shortage in the other processes, that the blow-room registers of the assessee clearly showed that it had consumed larger quantities of Khamgaon and Berar varieties of cotton and that making allowance for this factor there was increase of only 1.4 per cent. in the shortage as compared to the preceding year. The Appellate Assistant Commissioner, however, held that, though the addition made by the Income-tax Officer was not justified on the mere date of the blow-room loss, there was also no justification for the increased percentage of dead loss as shown by the assessee. Giving consideration for the increased loss from the use of different types of cotton, he estimated the value of unaccounted stock at Rs. 50,000 in place of Rs. 1 lakh. His order is made a part of the case and is marked annexure 'I'.

24. The assessee thereupon appealed to the Tribunal who confirmed the addition sustained by the Appellate Assistant Commissioner on ground detailed by the Appellate Assistant Commissioner. The order of the Tribunal is made a part of the case and is already marked annexure 'F'.

25. This case is stated as required by the Hon'ble High Court by reference to the two questions of law which have been stated in paragraph 1 above. The statement is agreed to by the parties."

26. We are concerned in this case only with respect to the assessment year 1949-50, corresponding to the account year ending Diwali 1948. The question arose whether the dead loss shown by the assessee in the year in question was properly assessed and whether on account of the inflation of the loss there was consequential suppression of production of yarn. The Income-tax Officer has described the various stages of process in the spinning department of the assessee-mills from the stage of raw cotton to the stage it comes out in the shape of yarn. The main sections of the spinning department are : (1) blowing, (2) carding, (3) slubbing, (4) inter, (5) roving, (6) ringframe and (7) reeling. Cotton freed of cotton seed is first mixed with some soft

waste and, after so mixing with soft waste, it is fed into the blowing section. From the blowing section, in which operation there is admittedly considerable loss, the cotton goes to the carding section and then to succeeding sections in the order in which it is enumerated above. Ultimately it comes out in the shape of yarn in the ringframe and reeling sections. In undergoing through all these stages a particular quantity of cotton always loses some of its weight before ultimately it is converted into the yarn. These losses in weight are under two categories called visible loss and invisible loss. What is described as visible loss consists of soft waste and hard waste, while the invisible loss consists of dust, leaves, etc. In other words, visible loss which comprises soft and hard waste will again be used for making the yarn. That yarn may be of an inferior variety. The name of dead loss is given to the invisible loss because nothing can be recovered from this loss. The assessee supplied statistical information regarding the quantity of cotton fed in the blowing section along with the waste and the quantity after coming out of the blowing section in the form of laps. Thereafter, there is no quantitative record of cotton passing through the further stages until it comes out as yarn without again losing its weight. Dead loss percentage of cotton is arrived at by deducting from the net cotton consumed the weight of yarn produced as well as soft waste received and the balance represents the weight or the percentage of dead loss in this procedure.

27. It is an admitted position that for the previous year, that is assessment year 1948-49, the percentage of dead loss was 7.9 per cent. and the percentage of total loss was 21 per cent. As regards the year in dispute the percentage of dead loss was 10.6 per cent., while the percentage of total loss was 22.7 per cent. The assessee explained the increase in the percentage of dead loss and also the total loss on the ground that they were acquired to purchase inferior cotton, such as cotton from Khamgaon and other Berar markets which had much more impurities, which impurities, according to the assessee, could not be separated in the blowing room operations and continued to affect the total quantity of weight of cotton which was available for being turned into the yarn. In other words, the assessee's case is that the increase in the percentage of dead loss as well as the overall loss was due to the inferior cotton.

28. The Income-tax Officer called upon the assessee to prove the actual loss in each section of the spinning department, that is, in section from the blowing section such as carding, slubbing, inter, roving, ringframe and reeling sections. The assessee was unable to produce these figures because no quantitative account could be maintained either for carding or subsequent stages through which cotton went before it ultimately came out in the shape of yarn. It does not seem to be disputed that once the cotton is fed in the carding section, it is a continuous process till it comes out as yarn and there is no break. It is on that account that the assessee claimed that it was not possible to have a quantitative record of the cotton in each section as it passes through each section. The figures of losses both visible and invisible actually occurring in the blowing section

were maintained by the assessee and were produced. It appears that the spinning master concerned was also examined and his statement has been taken into account by the Income-tax Officer. It was pointed out by this spinning master of the mill that out of the total invisible loss, that is, the dead loss, 90 per cent. occurs in the blowing room and carding section and the rest 10 per cent. is covered by other sections of the spinning department and out of the 90 per cent. loss more than two-third loss occurs in the blowing room. On behalf of the assessee statistical information about the findings of the Indian Cotton Research Institute in respect of the percentage of loss on the basis of experiments made by them was also produced.

29. The Income-tax Officer compared the loss percentages in respect of each of the three assessment years 1947-48, 1948-49 and 1949-50 so far as the blowing section is concerned and he pointed out that whereas in the earlier two years the visible and invisible loss percentage was 8.69 and 8.67 per cent respectively, it was reduced to 6.03 per cent. in the year in question, that is, in the assessment year 1949-50. In view of the actual percentage of loss available in the blowing room, the Income-tax Officer, felt that the experimental loss percentage of the public authorities which is derived from very small quantities furnished by the Indian Cotton Research Institute could not be a guiding factor in determining the actual percentage of loss which could be reasonably expected.

30. The Income-tax Officer also called upon the assessee to supply the quantities of yarn of particular count made from corresponding quantities of laps in the same court, but this information was also not given by the assessee because, as already stated, there was no quantitative record of laps once it entered the carding section being possible to be maintained. In view of these circumstances, the Income-tax Officer made a lump sum addition of Rs. 1,00,000 to cover for the loss of production of yarn and soft waste. In coming to this conclusion, the Income-tax Officer has observed as follows :

"In the circumstances stated above, the dead loss shown by the assessee cannot be taken as a correct one as the assessee has not been able to prove the actual dead loss. The losses actually suffered in the blowing room pointed really towards a better result as compared to last year. I would, therefore, make a lump sum addition of Rs. 1,00,000 to-cover for the loss of production of yarn and soft waste (in closing stock 1,44,000 lbs. of yarn are valued at Rs. 2,10,062). The addition roughly takes the percentage figures of production and dead loss of assessment year 1948-49 as a base, though the actual figures of losses in the blowing room point towards more production during the relevant assessment year."

31. Against this addition, the assessee preferred an appeal, among other grounds, before the appellate authority. The Appellate Assistant Commissioner dealt with the contention in respect of this addition in paragraph 8 as contention No. 7. The Appellate Assistant Commissioner has

observed that the Income-tax Officer found that the accounts were defective in that no sectional registers were maintained showing the losses in the various stages or departments of spinning and that therefore the overall losses claimed by the assessee could not be accepted as proved. The Appellate Assistant Commissioner has also referred to the view taken by the Income-tax Officer that on the basis of the increasingly favourable result as shown from the blowing room losses, the increase in overall losses in the account year is unlikely and must be evidently due to under-stand production of yarn and soft waste. The Appellate Assistant Commissioner apparently saw force in the explanation given by the assessee regarding the inability to keep account of weight in sectional registers for different stages because once mixed cotton is put in machine and goes in an unbroken chain through various stages of mechanical process till the cotton comes out from the machine as yarn. It was, therefore, inherently impossible to maintain sectional registers to prove the losses in the various stages or departments of spinning. The appellate authority has recorded a definite finding that the estimated addition by the Income-tax Officer on the mere data of the blowing room loss is not justified. The Appellate Assistant Commissioner also held that the technological reports of the Indian Central Cotton Committee which embody the results of scientific and laboratory tests cannot be brushed aside as was done by the Income-tax Officer by merely saying that the results shown by the tests of small quantity cannot be applied to bulk production. The Appellate Assistant Commissioner also seemed to take due notice of the fact as shown from the different types of cotton in the blowing room registers that inferior and poor qualities have been used in large quantities from Khamgaon and Bearer varieties than the previous years.

32. It appears, the assessee's representative filed a statement before the appellate authority showing how there would be at least an increase of 1.4 per cent. in the percentage of losses during the accounting year as compared to previous year, but even so, the Appellate Assistant Commissioner observed that a little margin for saving of losses on account of bulk production had to be given and all considered, he estimated the increased loss at one per cent. The Appellate Assistant Commissioner further observed that the dead loss percentage as compared with the previous year showed a much greater increase by 2.7 per cent. and that there was no justification for this increased percentage of dead loss. The Appellate Assistant Commissioner has observed that the percentage of dead loss on the basis of the technological reports stops with the blowing room and carding section, but it was pointed out by him that once the cotton was mixed up and processed into laps for slubbing, which operation stops with the blowing room and carding section, the loss percentage thereafter will be negligible from the mechanical processes. On this view of the matter, the Appellate Assistant Commissioner estimated the excessive and unproved loss at 1.7 per cent. and the value of the unaccounted stock at Rs. 50,000 on the basis of the controlled rates of yarn. He, therefore, gave reduction of Rs. 50,000 in the addition made for the Income-tax Officer.

33. When the matter went up before the Tribunal, the Tribunal does not seem to have applied its mind independently but seemed to accept what was stated by the Appellate Assistant Commissioner and confirmed his findings. They have reproduced the relevant portion from the order of the Appellate Assistant Commissioner and held that the Appellate Assistant Commissioner has carefully considered the explanation of the assessee and has given such reduction as was found to be rightly due to the assessee. In other words, they did not feel called upon to interfere with the order of the Appellate Assistant Commissioner in this respect.

34. As the Tribunal apparently did not make a reference in respect of the question now referred, the assessee approached this court and this court required the Tribunal to refer the question which has now been referred under section 66(2) of the Indian Income-tax Act, 1922, as already stated.

35. In support of this reference, it is strenuously contended on behalf of the assessee that no defect has been found in the method of accounting as maintained by the assessee in respect of the cotton used in different stages and the records kept regarding consumption of cotton and losses at different stages. It is pointed out that the calculation made by the authorities even for the purpose of making an addition are on the basis of figures furnished by the accounts kept by the assessee. So far as the weight of the total net cotton consumed was concerned, it was the weight of the yarn produced or the weight of the stock in process or the weight of the cotton after mixing. The contention, therefore, is that if the system of keeping accounts of cotton with regard to its weight as it passes through different stages is neither defective, nor could it be said that no method of accounting has been regularly employed, then it is incumbent on the income-tax authorities to compute the total production in accordance with the method of accounting regularly employed by the assessee. It is urged that the defect or failure attributed by the Income-tax Officer in not keeping quantitative records of weight at different stages of a continuous process, has not been upheld by the Appellate Assistant Commissioner. It could not, therefore, be said that the assessee has failed to keep regular accounts by the method consistently followed by the assessee in respect of the weight of cotton consumed. Unless there is a finding, the argument goes, which brings in the proviso to section 13 into play, it is not possible for the income-tax authorities to make an estimate of alleged production of yarn merely on the hypothesis that there has been a more percentage of invisible loss in a particular year. If such an estimate was permitted, it is urged, it will only amount to making addition on a hypothetical or arbitrary basis for which there is no material on record. It is also urged that there is an obvious error in the calculation made by the Appellate Assistant Commissioner in interpreting the statement of the spinning master about the percentage of overall losses. The contention of the assessee's is that the statement of the representative filed before the Appellate Assistant Commissioner referred to the overall loss and not loss in respect of a particular section. What was attempted to be proved was that even according to the estimate made on the basis of technological reports the percentage of overall

loss was 1.4 per cent., whereas according to the actual account and figures maintained in the books of the assessee, the difference between the previous year's overall loss and the overall loss in the year in question only came to 1.7 per cent. In the very nature of things, it is urged, it not being possible to record the loss, in particular the dead loss, once the cotton leaves, in the form of laps, the blowing room section, the assessee could not be penalised by an estimated addition in the yarn produced while accepting the figures of weight of cotton fed in the blowing room and also accepting the weight of yarn produced at the end of the spinning process. It is also pointed out that there is a certain confusion in mixing up the statement regarding the percentage of loss in the blowing room process and further processes. The figures available and which have been taken into consideration are in respect of percentage of loss only till the cotton comes out of the blowing room section. No figures being available regarding the percentage of the loss in the carding room section, it would be a mere speculation to say in respect of a particular year that the loss is more or less by any such estimate. It is also urged that the basis taken by the Income-tax Officer for making the addition on the ground that there was actually a decrease in the percentage of loss in the blowing section in question has been erroneously interpreted inasmuch as the assessee being required to use inferior cotton, the impurities which could be blown off in the blowing room process would be less than when a superior type of cotton was used. On account of the inferior and poor quality of cotton employed, the impurities could not be separated in the blowing room process. In view of this position, it having been accepted by the Appellate Assistant Commissioner that increase in percentage of loss was due to the use of inferior cotton from Khamgaon and Berar District supplies, the explanation given by the assessee about the increase in the percentage of loss should have been accepted as reasonable and probable. As regards the statement of the spinning master that the major percentage of loss to the extent of 90 per cent. is in the blowing room and the carding section has not been correctly interpreted inasmuch as the actual losses in the carding section are not available according to the records and those losses are also considerable in view of the poor quality of cotton used in that year.

36. In this connection, our attention was invited to certain decisions. *Arumugaswami Nadar v. Commissioner of Income-tax* is the decision of the Madras High Court. In this case, in reassessment proceedings of the assessee who carried on the business of match manufacturing by manual process, the Income-tax Officer felt that the consumption of chlorate as shown by the records was excessive and on that view added an extra amount by way of income escaping assessment on the ground that the consumption of chlorate as shown by the assessee was excessive. It was held that in view of the difficulties obtaining in the manual manufacture of matches as found by the Appellate Tribunal, the maintenance of a daily mixture account could not possibly help in the correlation of the issue of chlorate with the manufacture of matches. Such a maintenance of record was not insisted by the department at any earlier stage and the High Court held that the conclusion that the book results were not reliable could not be reached

for want of maintenance of this record.

37. In this case, the petitioner-assessee, on a parity of reasoning, says that it not having been practicable or possible to maintain quantitative record of losses, that is, dead losses, once the cotton leaves the blowing room section, that book figures of losses according to the method possible to be adopted could not be lightly ignored or rejected. It is also urged that the other public authorities such as the Textile Commissioner and the excise authorities are required periodically to inspect the records and keep a watch at different stages of production to ensure that there is no infraction of the liability for excise duties or other provisions of the Textile Control Order. In none of these reports there is any suggestion that there was a suppression of production of yarn or deviation therefrom. This fact was also taken into consideration by the Madras High Court decision which held that the assessee was entitled to rely on the fact of these periodical checks not having noticed any suppression to show that in so far as the book results were concerned what has been sold was actually accounted for.

38. The next case is *Pandit Bros. v. Commissioner of Income-tax*. The assessee was carrying on business and had maintained regular accounts on the basis of which a statement of profit and loss was filed. The Income-tax Officer added a certain sum on the ground that the profits disclosed as per accounts were low and also because there was no stock register. It was held that, in the absence of a definite finding by the Income-tax Officer that the case fell within the proviso to section 13, it was not possible to sustain the addition of the profits and the mere fact that the profits were low is not a circumstance or material aliunde which could justify an estimate in these circumstances.

39. *S. Veeriah Reddiar v. Commissioner of Income-tax* is the next case relied on which directly arose under section 13 of the Indian Income-tax Act, 1922. The court took the view that no assessment under the proviso to section 13 could be sustained if the Income-tax Officer has not considered and recorded a finding against the assessee as to whether he has been regularly employing a method of account. What can be said in the instant case, it is urged, was somewhat similar approach when the case was before the Income-tax Officer, and that was by sole reason of the fact that quantitative record of losses or wastage was not kept at subsequent stages once the cotton went out of the blow-room section. But if it is not possible to keep such record and which position seems to be realised by the Appellate Assistant Commissioner, there was no other reason not to accept the book results of the records kept by the assessee and if there were no materials not to accept the regularly kept record, it is contended, the addition by way of estimate in this case was not permissible.

40. The learned counsel, appearing for the revenue, dispute that this is a case covered by the proviso to section 13 of the Indian Income-tax Act. According to him, the proviso cannot be

called in aid and has not been relied upon and none of the cases based on the interpretation and requirement of section 13 are relevant. According to the learned counsel, the statement made by the representative of the assessee and the spinning master was the material on which the income-tax authorities have come to certain conclusions. If that is the material which could be relied upon to come to that conclusion, then it cannot be said that there was no material on which the conclusion could not be reached. Once the department is able to show that there was such material, this court will not go into the question whether the amount that has been added has been properly added or not because that was the question which was referred.

41. In our opinion, the material which is pointed out and to which reference is made in the order of the Appellate Assistant Commissioner in paragraph 8 of his order cannot be considered de hors the context. The difficulty that seems to have arisen in this case is that by the very nature of the spinning process the cotton being required to pass through different sections in a continuous process, it cannot be predicted what would be the percentage of losses at stages subsequent to the blowing room section. Merely by comparison of the percentage of losses in a particular year, we do not think it is possible to say with any reasonable certainty that the increase in the percentage of loss must be attributable and must lead to a reasonable inference of suppression of production of yarn. It having been accepted that inferior cotton was used and it also being accepted that it is not possible to have separate quantitative record of percentage of loss at stages subsequent to the blowing room section, it will amount to mere speculation to say that the loss should not be of a particular order after the cotton goes out of that section. The statement of the representative also, it appears to us, has not been considered in its proper context. The Appellate Assistant Commissioner ultimately was required to observe :

"All considered I shall estimate the increased loss to be about 1 per cent."

42. To hold it could be considered one per cent. or 1.4 per cent. or 1.7 per cent., he has not referred to any material on record. The Appellate Assistant Commissioner has observed that the increase of 2.7 per cent. in the percentage of losses till the cotton comes out of the blowing section is not justified. We are unable to reconcile this statement with the acceptance of the fact that inferior cotton had to be used. The Appellate Assistant Commissioner has observed that the increased percentage of losses on the basis of the technological reports stops with the blowing room and carding section and yet states that it should be noted that when once the cotton has been mixed up and processed into laps for slubbing, which operations stop with the blowing room and carding section, the loss percentage thereafter will be negligible from the mechanical process. For this observation, again, we do not find any material on record and that is because of the fact that there was no record of the losses in the carding room section or subsequent sections. With regard to the statement of the spinning master that 90 per cent. of the losses were in the

blowing and carding section and that only 10 per cent. was in the other sections, before the assessee could be charged with the exaggeration of losses at stages subsequent to the blowing room section, one should have expected some material on record to justify such a conclusion. In our opinion, there is no such material.

43. We are also unable to accept the contention that the principle of section 13 of the Income-tax Act are not attracted in this case. The assessee has followed a regular method of keeping account of the cotton consumed in the whole of the spinning process. It is not shown that there is any other or better method of keeping account of such consumption. In fact, it does not appear to be disputed that the quantity of cotton shown to be consumed is not more than what has been found from the figures in the assessee's books. The ultimate conclusion is reached only on the basis of the alleged exaggeration in the percentage of dead losses. If there is no material on which it could be established that the increase in the percentage was attributable to any suppression of weight or any suppression of production, then we fail to see how the right under the proviso could be availed of by the Income-tax Officer in making an estimate. The very condition for making use of the right under the proviso arises after the findings is recorded as to the non-acceptability of the method and irregularity of the accounts kept. It does not appear that there is such a finding recorded by the authorities in this case; in the absence of such a finding the book result could not be ignored or brushed aside. The mere fact that the percentage of loss is very low in a particular year cannot possibly lead to an inference that thereby there has been a suppression in the weight of yarn that is produced. We are not satisfied that on the material on record that the sum of Rs. 50,000 could be included in the total income of the assessee on account of the alleged understated production of yarn and soft waste. We, therefore, answer the second question referred to us in the negative and in favour of the assessee.

44. The third question that arises and that has been referred to is relevant only in Income-tax Reference No. 6 of 1966 and that question is :

"Whether the expenses for preparing return, etc., and representation before the Income-tax Officer (Rs. 589) and expenses connected with appeals to the Tribunal (Rs. 3,048) are admissible in computing the income of the assessee ?"

45. This question has been referred by the Tribunal as a result of the application under section 66(1) of the Indian Income-tax Act made by the assessee for the assessment years 1955-56 and 1956-57.

46. A large number of decisions have been cited before us and, on behalf of the department, naturally, the decision of this court in *S. D. Sharma v. Commissioner of Income-tax* has been relied upon. On the other hand, since that decision was given, the matter has been considered be

different High Court and at least by two courts, namely, Madhya Pradesh and Calcutta High Courts, a contrary view has been taken. The question often arises as to the allowability of litigation expenses incurred by an assessee for the purpose of his business or trade. Some kind of litigation expenses have been allowed but not others. English decisions which have governed the main scheme of approach in this case have also undergone a certain change. Expenses incurred by an assessee indirectly connected with the trade but incurred with a view to prosecute the trade or business or to foster trade have been allowed. Thus in *Commissioner of Income-tax v. Royal Calcutta Turf Club*, the Supreme Court affirmed the decision of the Calcutta High Court in allowing expenses for running a school for training jockeys. The direct case in point is in *Binodiram Balchand v. Commissioner of Income-tax*, where the claim for allowance of professional fees paid to an income-tax adviser has been accepted. The claim for expenses of a lawyer for defending in a criminal case resulting in acquittal has been accepted by the Patna High Court in *Rohtas Industries Ltd. v. Commissioner of Income-tax*. Another decision of the Calcutta High Court in *Birla Cotton Spinning and Weaving Mills Ltd. v. Commissioner of Income-tax*, allows lawyer's expenses for making representation before the Income-tax Investigation Commission. In yet another decision in *Sree Meenakshi Mills Ltd. v. Commissioner of Income-tax*, the Supreme Court observes at page 213 as follows :

"Under section 10(2) (xv) of the Indian Income-tax Act, as amended by Act 7 of 1939, expenditure even though not directly related to the earning of income may still be admissible as a deduction. Expenditure on civil litigation commenced or carried on by an assessee for protecting the business is admissible as expenditure under section 10(2) (xv) provided other conditions are fulfilled, even though the expenditure does not directly relate to the earning of income. Expenditure incurred not with a view to the direct and immediate benefit for purposes of commercial expediency and in order indirectly to facilitate the carrying on of the business is therefore expenditure laid out wholly and exclusively for the purposes of the trade."

47. Referring to their own decision in *Commissioner of Income-tax v. H. Hirjee* the Supreme Court has observed as follows :

"It was held by this court in *Commissioner of Income-tax v. H. Hirjee* that the deductibility of expenditure under section 10(2) (xv) must depend on the nature and purpose of the legal proceeding in relation to the business whose profits are under computation and cannot be affected by the final outcome of that proceeding. The proceeding started by the company was in relation to the business of the company. The company was thereby seeking relief against interference by the executive authorities in the conduct of its business in the manner in which it was being carried on previously. It

was also seeking to obtain an order for restoration of its goods which were seized. It may be granted that the company was, in starting the proceeding, ill-advised. However wrong-headed, ill-advised, unduly optimistic or over-confident in his conviction the assessee may appear in the light of the ultimate decision, expenditure in starting and prosecuting the proceeding may not be denied admission as a permissible deduction in computing the taxable income, merely because the proceeding has failed, if otherwise the expenditure is laid out for the purpose of the business wholly and exclusively, i.e., reasonably and honestly incurred to promote the interest of the business."

48. In the decision of the Punjab High Court in *J. N. Singh & Co. (P.) Ltd. v. Commissioner of Income-tax*, expenses in conducting a criminal prosecution had also been allowed.

49. In view of the different facts which arises for consideration in considering the claim for allowance in respect of an expenditure under section 10(2) (xv) of the Income-tax Act, in our opinion, this is a question which should be considered by a larger Bench. If one kind of expenses of litigation are allowable, the mere fact that the expenses are claimed in respect of income-tax proceedings may not necessarily be a bar to the allowance if it can be established that the expenses were incurred in connection with the business. It may be many a time a principle is involved or an interpretation of an important question is involved, which is bound to affect the assessee's trade not only in the year in question but for years to come. Therefore, it may be possible to hold uniformly in all cases that the amounts spent on advice, or engaging services of an expert or prosecuting an appeal or proceeding under the Income-tax Act is necessarily an expenditure which cannot be allowed in all cases. In our opinion, therefore, this is a question which should better be considered by a larger Bench in the context of the subsequent pronouncements made by different High Courts and also by the Supreme Court. So far as this question is concerned, therefore, we direct that the papers may be placed before My Lord the Chief Justice for suitable orders.

50. So far as the question No. 1 is concerned, it is answered in favour of the assessee. There does not appear to be any impediment in the assessment proceedings being further taken in hand in the light of this decision in all the years. So far as the question No. 2 is concerned, it relates only to one year and that is also finally answered so far as this court is concerned. So far as the third question is concerned, which arises in one case, in view of the fact that it may be considered by a larger Bench, we need not hold up action being taken in pursuance of the answers to the other two questions. The said questions are answered accordingly. The assessee will be entitled to costs in all the cases.



