



IN THE HIGH COURT OF JUDICATURE AT BOMBAY

ORDINARY ORIGINAL CIVIL JURISDICTION

INCOME TAX APPEAL NO.744 OF 2002

The Indian Hume Pipe Co. Ltd.
Construction House,
Walchand Hirachand Marg,
Ballard Estate,
Mumbai – 400 001

.. Appellant

Versus

Commissioner of Income Tax,
Central II, Aayakar Bhavan,
M.K. Road,
Mumbai – 400 020.

.. Respondent

Mr.S.Sriram a/w Mr.B.V. Jhaveri & Ms.Bhargavi Raval for Appellant.
Mr.Suresh Kumar for Respondent.

CORAM : **G.S. KULKARNI &
JITENDRA JAIN, JJ.**
RESERVED ON : **3rd AUGUST 2023**
PRONOUNCED ON : **31st AUGUST 2023**

Judgment (per Jitendra Jain, J.) :-

. This consolidated appeal is filed by the Appellant Assessee for assessment years 1986-87, 1987-88 and 1988-89 against common order passed for these three years by the Income Tax Appellate Tribunal (for short “Tribunal”) dated 18th January 2002. The present appeal was admitted under Section 268A of the Income Tax Act, 1961, for short (the Act”) by this Court on 10th September 2004 on the following substantial

question of law :-

Substantial question of law

“Whether on the facts and in the circumstances of the case, the Appellate Tribunal’s conclusion that the commission agents had not rendered services to the Appellant company to warrant payment of commission is based on relevant and valid material and is sustainable in law ?”

2. The facts for the assessment year 1986-87, being the lead year, are taken as the basis for deciding the present appeal.

Brief facts are as under :-

3. The Appellant is a limited company listed on the stock exchange and is engaged mainly in the business of manufacturing and sale of R.C.C. Pipes, Steel Pipes etc. which are required for water supply and drainage system.

4. On 30th June 1986, the Appellant filed its return of income declaring income of Rs. 1,89,85,950/-. The said return was supported by audited financial as per the Companies Act and tax audit report as per Section 44AB of the Act. The said return was selected for scrutiny assessment by issuing a notice under Section 143(2) of the Act.

5. In the course of the assessment proceedings, the Appellant

filed details of commission paid amounting to Rs. 26,90,104/-, which are as under:-

1.	M/s. J.R.D. Legal Metal Industries Pvt. Ltd. Udaipur	11,44,920/-
2.	Metson Metal & Chemicals	3,13,460/-
3.	M/s. Chintambi & Swaminathan, Hyderabad	2,80,000/-
4.	A. Mohan Menon	1,82,807/-
5.	M/s. Manyam Engg. Enterprises, Hyderabad	4,50,000/-
6.	M/s. Dhanashree Textiles	1,93,437/-
7.	M/s. Middle East Construction Co.	79,577/-
8.	M/s. Universal Supply Corp., Jaipur	45,903/-
		===== 26,90,104/-

6. The Appellant Assessee also filed copies of the agreements with the aforesaid parties and justified the allowability of the commission payment as business expenditure incurred in course of its business.

7. On 30th June, 1985, an assessment order under Section 143(3) of the Act was passed assessing income at Rs. 2,89,64,500/-. In the said assessment order, various additions/disallowances were made. The Assessing Officer disallowed a sum of Rs. 22,89,941/- on account of commission payment claimed as deduction by the Appellant Assessee.

8. Insofar as commission paid to M/s. Chintambi &

Swaminathan, Hyderabad, A. Mohan Menon and M/s. Manyam Engg. Enterprises, Hyderabad is concerned, the Assessing Officer disallowed whole of the amount and with respect to balance parties, the Assessing Officer allowed only 1/3rd as deductible expenditure and disallowed balance 2/3rd on the ground that the entire payment cannot be considered as laid out wholly and exclusively for the purpose of the business because neither the Appellant Assessee nor the recipients of commission could show that orders were procured with their assistance. Therefore, the role of commission agent is only in respect of follow up enquiries and therefore, only 1/3rd was considered as deductible expenditure.

9. Being aggrieved by the aforesaid assessment order, the Appellant Assessee preferred an appeal to the Commissioner of the Income Tax (Appeals)-II, Bombay. On 31st January, 1992, the Commissioner (Appeals) disposed of the said appeal. With respect to ground relating to disallowance of commission payment, the Commissioner (Appeals) followed his own order for assessment year 1985-86 and allowed the whole of the amount which was disallowed by the Assessing Officer, that is, Rs.22,89,941/-. Insofar as other grounds are concerned, the Appellant Assessee got reliefs on some of the grounds and therefore the appeal was partly allowed.

10. Being aggrieved by the aforesaid order, the Respondent Revenue filed an appeal to the Tribunal and the said appeal was numbered as ITA '3141/Bom/92.' In the said appeal the Revenue challenged various grounds on which the Commissioner (Appeals) gave relief including ground relating to commission payment. The Tribunal disposed of the said appeal on 18th January, 2002. With respect to M/s. Chintambi & Swaminathan and M/s. Manyam Engineering Enterprises relating to the commission payment, the Tribunal restricted disallowances to 2/3rd of the total commission. With respect to A. Mohan Menon, the Tribunal directed to give relief of 1/3rd of the amount of Rs. 1.40 lakhs, since the said party admitted to have received an amount of Rs. 1.40 lakhs and the Appellant Assessee has not brought on record any material to explain the discrepancy in the amount shown to have been paid by the Appellant Assessee of Rs.1,82,807/- and admitted to have been received by the recipient. With respect to other remaining parties, the Tribunal confirmed the disallowance made by the Assessing Officer on the ground that the Appellant Assessee did not furnish any evidence in support of services rendered by these commission agents. The Tribunal further observed that there should have been lot of correspondence between the Appellant Assessee and the recipient of commission and in absence of any evidence in this regard,

the disallowance made by the Assessing Officer was justified. Being aggrieved by the Tribunal's order, the Appellant Assessee has filed present appeal on a substantial question of law which was formulated by this Court on 10th September, 2004.

11. Heard learned counsel for the Appellant and the Respondent and with the assistance of the counsel, we have perused the records annexed to the appeal memo.

Submissions of the Appellant Assessee :-

12. The Appellant Assessee submitted that on an identical issue on similar facts in the assessment year 1985-86 that is immediately the preceding year, disallowance was made by the Assessing Officer on a very similar ground and Commissioner (Appeals) on this issue for the said assessment year granted relief to the Appellant and the said order of the Commissioner (Appeals) was not challenged before the Tribunal and therefore, the facts being identical in the year under consideration, based on the principles of consistencies, the commission payment ought to have been allowed as business expenditure.

13. The Appellant Assessee further contended that the commission agents are not related to the Appellant and further they

have also produced the commission agreements with these agents in course of the assessment proceedings. The payments have been made through banking channel and there is no allegation that payments made to the commission agent has come back to the Appellant. The Appellant further submitted that nature of services are such that there would not be any documentary evidence in support thereof.

14. In support of the aforesaid submissions, the Appellant Assessee relied on the following case laws:-

- i. *Radhasowami Satsang V/s. CIT [1992] 193 ITR 321 (SC).*
- ii. *Aluminium Corporation of India Ltd. V/s. CIT [1972] 86 ITR 11 (SC).*
- iii. *PCIT V/s. Quest Investment Advisory (P) Ltd. [2019] 409 ITR 545 (Bom).*
- iv. *CIT V/s. Dalmia Promoters Developers (P) Ltd. [2006] 281 ITR 346 (Del).*
- v. *CIT V/s. M/s. Motilal Duli Chand Income Tax Appeal No.97 of 2002 (All. HC).*
- vi. *DCIT V/s. Super Tannery (India) Ltd. [2005] 274 ITR 338 (All).*
- vii. *CIT V/s. Noshira Dara Mody [2014] 50 taxmann.com 193 (Bom).*

15. The Appellant Assessee, therefore, prayed that the Tribunal's order reversing Commissioner (Appeals) order on this issue is to be reversed.

Submissions of the Respondent Revenue:-

16. The Respondent Revenue contended that the Appellant Assessee has failed to furnish any evidence to show that services have been rendered and therefore, the Assessing Officer was justified in disallowing the commission.

17. The Respondent further contended that these are findings of facts recorded by the lower authority and the same could not be interfered with by this Court under Section 260A of the Act. The Respondent further submitted that the findings of the Tribunal are based on appreciation of evidence and therefore there does not arise any question of law much less substantial question of law. The Respondent also brought to the notice of the Court Explanation 1 to Section 37(1) of the Act which was introduced by the Finance No. 2 Act of 1998 with retrospective w.e.f. 1st April, 1962. However, he fairly submitted that in the present appeal the case of the Revenue is not based on Explanation. The Respondent, therefore, supported the orders of the Assessing Officer and the Tribunal and prayed for dismissal of appeal.

Analysis:

18. The Assessing Officer with respect to items at serial nos.1, 2 and 6 to 8 reproduced hereinabove are concerned disallowed 2/3rd of

the commission payment on the ground that the Appellant-Assessee could not furnish evidence about the services having being rendered. With respect to Item Nos.3, 4 and 5 disallowed whole of the commission payment on the ground that they were acting as sub-contractors to the Appellant-Assessee and therefore no question arises to make payment of commission to these parties. With respect to Mr. Mohan Menon, there was discrepancy in the figures paid by the Appellant-Assessee and confirmed by the recipient and therefore full amount was disallowed. The said disallowance was fully deleted by the First Appellate Authority. However, on the Revenue's appeal to the Tribunal, the Tribunal has confirmed 2/3rd disallowance with respect to parties at serial nos.1, 2 and 6 to 8, made by the Assessing Officer. Similarly, with respect to parties at serial nos.3, 4 and 5, the Tribunal partly confirmed the disallowance made by the Assessing Officer. The above findings of the Assessing Officer and the Tribunal indicates that both the authorities have not fully disallowed the commission payment but as partly allowed (1/3rd) and partly disallowed (2/3rd). If that be so, then the lower authorities have accepted the rendering of service by the commission agent and it is only on that basis that 1/3rd came to be allowed by the Assessing Officer and the Tribunal. In our view, the services are either rendered or not rendered and the Assessing Officer and the Tribunal

having allowed partly the commission payment clearly indicates that both the authorities have accepted that the services have been rendered. The part disallowance confirmed by the Tribunal and the Assessing Officer would then amount to the Revenue venturing into the quantum of payment whether the commission payment was reasonable for rendering the services, which course of action, in the facts of the present case, is not permissible under the Act because the transaction is between unrelated parties. It is a settled position that the Revenue cannot sit in judgment over the assessee to come to a conclusion, how much payment should be made for the services received by the Appellant-Assessee. Therefore, in our view, the Tribunal was not justified in confirming the disallowance of 2/3rd as made by the Assessing Officer and allowing the relief of only 1/3rd of the expenses.

19. It is also important to note that there is no allegation made in the assessment order of any flow back of the commission payment by the commission agent to the Appellant-Assessee nor it is contended so before us. The commission agents have confirmed the receipt of the commission. The payments have been made through banking channels. Therefore, even on this account, the genuineness of the payment coupled with our observation made hereinabove cannot be doubted.

20. We have perused the agreement which are annexed at pages 148 to 159 of the appeal paper book. On a perusal of this agreement, the rate of commission is fixed at a certain percentage of the value of the work secured by the Appellant-Assessee with the assistance of these commission agent, however, the actual payment is made in installments/tranches based on the events mentioned in the commission agency agreement. For example, in the agreement dated 20th August 1973, with M/s. Middle East Construction and Equipment Pvt. Ltd., the rate of commission is fixed at 3% of the total value of work secured by the Appellant-Assessee. However, the payment of said 3% is in 2 tranches, namely, 2% will be paid on receipt of 15% advance received as per the tender and the balance 1% will be paid against receipt of each running bill and the final settlement or adjustment will be made after final bills are paid by the parties, who had floated the tender. Therefore, in our view, the assessee and the Tribunal was not justified in bifurcating the commission payment as between the work done for assisting in getting the tender and against follow up action for obtaining the payment. The agreement has to be read as a whole and merely because the payment of the commission is deferred in tranches, it could not be said that partly the payments are justified and partly are not justified. The action of the Assessing Officer and the Tribunal on this account would amount to

rewriting of the agency agreement which is not permissible. Therefore, in our view, the finding of the officer and the Tribunal for disallowing part of the commission payment on the above basis is also not justified.

21. The Appellant-Assessee is in the business, which inter alia involves contracts/works awarded by public sector/government, which necessitates the Appellant to apply for various tenders issued by the public sector co./government across the country. To apply for such public tenders the Appellant is required to engage the services of agents. As per the commission agency agreement, the services rendered by the commission agent is for supplying information for working out tender and to give information about the competitive tenders. The said agreement further requires commission agent to keep the Appellant-Assessee informed about various clarifications required by the companies who floated the tenders. The role of the commission agent does not stop at this, but if the Appellant-Assessee gets the contract, then the commission agent has to follow up with these corporations for realizing the payments on account of bills raised by the Appellant-Assessee. It is for such composite services to be rendered by the commission agent that the Appellant-Assessee makes payment of the commission. In our view, merely because the contracts awarded to the Appellant is by Government/ Public Corporations that does not mean that the

Appellant-Assessee cannot obtain services of the commission agents to assist them in the tendering process and for follow up action for recovery of the money, as for the Appellant it is fully a commercial activity and engaging expert/specialised services is under a written contract is entered between the commission agents and the Appellant. It is not the case of the Revenue that there is any legal prohibition for the Appellant-Assessee to avail services of such commission agents. It is also not the case of the Revenue that these commission agents within the meaning of the Act are entities/persons related to the Appellant-Assessee and/or they are government employees. Therefore, in our view, it is the business prerogative of the Appellant-Assessee as to whose services they should engage in the course of its business and on what terms and conditions. Most significantly, the fact that the Assessing Officer and the Tribunal have allowed part of the commission payment for the purpose of business also indicates that the Revenue has accepted the services rendered by and this part of expenditure in that regard was held to be allowable. There cannot be a contradictory course of action as the Revenue needs to be consistent.

22. It is true that it is for the Assessing Officer to decide, whether, any commission paid by the Appellant-Assessee to his agents are wholly or exclusively for the purpose of his business and the mere

fact that the Appellant-Assessee establishes the existence of an agreement between him and his agent and the fact of actual payment, the discretion of an officer to consider, whether such expenditure was made exclusively for the purpose of the business is not taken away. The expenditure incurred must be for commercial expediency. However, 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 businessman's point of view and not from the Revenue's perspective. In **J. K. Wollen Manufacturers Vs. Commissioner of Income Tax**¹, after applying the rule laid down in **CIT Vs. Walchand & Company Pvt. Ltd.**², the Supreme Court observed “.... *it is, of course, open to the 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 a trader or it is not laid down 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.’*” The Revenue also before us have not contested this position in law, which of course is quite settled. In the present case, the Assessing Officer and the Tribunal have allowed part of

1 1969 (1) SCR 525,

2 1967 (3) SCR 214 (SC)

the expenditure as business expenditure. The sequitur of this would be that insofar as the disallowance part is concerned, the Assessing Officer and the Tribunal would be venturing into the quantum of the expenditure which as laid down by the Supreme Court is not permissible.

23. ***Conclusion:-*** For the aforesaid reasons, we are of the view that the Assessing Officer and the Tribunal were not justified in disallowing part of the commission payment for the assessment years 1986-87, 1987-88 and 1988-89. In view thereof, the appeal of the Assessee is allowed by answering the question of law in favour of the Assessee and against the Revenue.

JITENDRA JAIN, J.

G. S. KULKARNI, J.