

IN THE HIGH COURT OF JUDICATURE AT BOMBAY

ORDINARY ORIGINAL CIVIL JURISDICTION

INCOME TAX APPEAL NO.273 OF 2007

The Commissioner of Income-tax
Aayakar Bhavan, Near Holi Cross
High School, Cantonment, Aurangabad. ..Appellant.

V/s.

Samarth Sahakari Sakhar Karkhana Ltd.
Wadigodri Tq.Ambad, Dist. Jalna. ..Respondent.

Mr.B.M.Chatterji with Mrs.P.P.Bhosale for appellant.

Mr.S.N.Inamdar with A.K.Jasani for respondent.

CORAM : F.I.REBELLO AND
J.P.DEVADHAR, JJ.

DATED : 17TH SEPTEMBER, 2007.

ORAL JUDGMENT (PER J.P.DEVADHAR, J.)

1. This appeal is filed by Commissioner of Income Tax, Aurangabad against the order of the ITAT dated 13/1/2006 in ITA No.564/PN/2005 relating to the assessment year 1995-96.

2. The appeal is admitted on the following substantial questions of law:-

- A) Whether on the facts and in the circumstances of the case, the Tribunal was justified in holding that the advances paid to the harvesting transport contractors was in the nature of business interest of the respondent and not a diversion of borrowed funds for non business purposes, even though such advance was not made in the normal course of business and was made without any specific contractual obligations and such payments were made out of the borrowings on which the respondent was paying higher interest to the financial institutions ?
- B) Whether on the facts and in the circumstances of the case, the Tribunal was justified in holding that Bakshish payment made by the respondent to the harvesting and transport labourers was out of the commercial expediency, when in fact such payments are purely voluntary, based on sweet will of the respondent and the said payment being over and above the agreed price under contract, could not be said to be a business expenditure ?
3. The appeal is taken up for final hearing by consent of both the parties.
4. In the assessment year in question, the assessing officer made disallowance of notional interest on the ground that the respondent-society ('assessee' for short) has diverted the interest bearing funds to harvesting and transport contractors ('H & T contractors' for short) at a lower rate of interest than the rate of interest paid by them on the borrowed funds. Similarly, the assessing officer made disallowances of claim on account of Bakshish paid by the assessee to the labourers employed by the H & T contractors.

5. On appeal filed by the assessee, the Commissioner of Income Tax (A) upheld the disallowance made by the assessing officer. On further appeal filed by the assessee, the Tribunal following its earlier decision allowed the claim of the assessee and deleted the disallowances by holding that the expenditure incurred by the assessee was on account of commercial expediency. Challenging the said order of the Tribunal, the revenue has filed the present appeal.

6. Mr.Chatterji, learned counsel for the revenue submitted that the rate and the commission payable by the assessee to the H & T contractors for harvesting and transporting sugar-cane from the field to the factory, are decided by the tripartite agreement entered into by and between the assessee, the State Government and the H & T contractors after extensive bargaining. Once the rate and commission payable to the H & T contractors is determined, there is no business expediency to make any advance payment to the H & T contractors. He submitted that in the absence of any clause in the tripartite agreement requiring the assessee to give advances, it was not obligatory for the assessee to advance loans to the H & T contractors at a lower rate of interest. Thus, the advance payment made to the H & T contractors was nothing but diversion

of borrowed funds. Since the assessee had borrowed funds at a higher rate of interest and had advanced it to the H & T contractors at a lower rate of interest without there being any obligation to do so, the assessing officer was justified in disallowing the proportionate interest payable on borrowed funds advanced to the H & T contractors and the Tribunal was in error in deleting the disallowance made by the assessing officer.

7. Mr.Chatterji further submitted that the Bakshish given by the assessee to the employees of the H & T contractors was also not covered by the tripartite agreement and, therefore, the said payment made voluntarily could not be allowed as business expenditure. He submitted that during the assessment proceedings, an opportunity was given to the assessee to explain as to why Bakshish claim of Rs.2,73,000/- should not be disallowed since it was not part and parcel of the agreement entered into by the assessee with the H & T contractors. As the assessee failed to submit its explanation and the Bakshish payment was based on the sweet will of the assessee and not based on any legal obligations, the said payment could not be said to have been made on account of business expediency. Expenditure incurred arbitrarily without any contractual obligation cannot be allowed as

business expenditure. Accordingly, Mr.Chatterji submitted that the questions framed above be answered in favour of the revenue.

8. Mr.Inamdar, learned counsel appearing on behalf of the respondent, on the other hand, submitted that making advance payment to the H & T contractors and giving Bakshish to the employees of the H & T contractors has been the general practice prevailing in the State of Maharashtra for several decades and such expenditure has been consistently allowed as business expenditure not only in the case of the assessee but also in the case of several other sugar factories. In support of the above contention, Mr.Inamdar tendered two affidavits annexing thereto the assessment orders relating to A.Y. 1988-89, 1989-90, 1990-91 and 1991-92 in the case of the assessee and the assessment orders relating to A.Y. 1985-86, 1986-87, 1987-88, 1988-89, 1989-90 and 1990-91 in the case of Rajarambapu Sahakari Sakhar Kharkhana Ltd. wherein similar claims have been allowed by the respective assessing officer and the said assessments have attained finality.

9. Mr.Inamdar further submitted that to achieve higher yield of sugar, it is essential that the sugar-cane after it is harvested is transported to the factory for crushing expeditiously. Any delay in

transporting the harvested sugar-cane results in reduction of sugar content. Wherever, H & T contractors express financial difficulty, to tide over the situation sometimes amounts are advanced to the H & T contractors at nominal rate of interest. Similarly, as the labourers employed by H & T contractors are required to do the harvesting and transportation work during adverse climatic conditions, Bakshish is given to them in the sum of Rs.200/- to Rs.250/- per head as incentives to continue with the work. This has been the uniform practice followed by the sugar factories all over Maharashtra and accepted by the income tax authorities for decades. Accordingly, Mr.Inamdar submitted that the advances paid to the H & T contractors and the Bakshish paid to the employees of the H & T contractors are expenses incurred for business purposes of the assessee and the same has been rightly allowed by the Tribunal.

10. Relying upon the decisions of the Apex Court in the case of **Shahzada Nand and Sons V/s. Commissioner of Income Tax (108 I.T.R. 358)**, **Sassoon J. David & Co. P. Ltd. V/s. Commissioner of Income Tax (118 I.T.R. 261)** and the decision of this Court in the case of **Tata Sons Ltd. V/s. Commissioner of Income Tax (18 I.T.R. 460)**, Mr.Inamdar submitted that in the context of the current socio economic thinking

which places general interest of the community above personal interest of the individual, the expenditure incurred by giving advances to H & T contractors and giving Bakshish to the employees of the H & T contractors with a view to receiving prompt supply of harvested sugar-cane is an expenditure incurred on account of commercial expediency and accordingly, the order passed by the Tribunal is liable to be upheld.

11. We have carefully considered the rival submissions. As per the tripartite agreement, H & T contractors transport the harvested sugar-cane to the factory at the rate and commission mutually agreed, between the parties. During the year, if the H & T contractors due to some financial difficulty seek loan, then the assessee advances some amount to them at a nominal rate of interest. The amount so advanced is ultimately adjusted from the amount payable to the H & T contractors under the tripartite agreement. The question is where the funds borrowed at a higher rate of interest are advanced as a loan at a lesser rate of interest, whether differential interest can be disallowed on the ground that the borrowed funds have been diverted for non business purposes ? The Tribunal has held that such advances given by the assessee to H & T contractors was in the business interest of the assessee. Admittedly, the entire business of the

assessee during the crushing season depends upon the timely supply of the harvested sugar-cane by the H & T contractors. Therefore, giving some amount in advance to meet the exigencies of the H & T contractor would be certainly in the business interest of the assessee. It is pertinent to note that during the assessment year in question, the total amount paid to the H & T contractors is Rs.2,91,74,808.23 and commission paid to the H & T contractors is Rs.33,36,110.70, whereas the advance given to the H & T contractors during the year at a lower rate of interest is only Rs.26,88,114/-. If the H & T contractors require some amount in advance to mobilise the labour force or otherwise, not giving such advances will not be in the interest of the assessee's business. Due to paucity of funds if the contractors are unable to transport the sugar-cane promptly, then the sufferer would be the assessee. In these circumstances, the finding recorded by the Tribunal that giving some amount in advance to the H & T contractors was in the business interest of the Society cannot be faulted.

12. The fact that the assessee has given such advances to the H & T contractors at a lower rate of interest cannot be a ground to hold that the borrowed funds have been diverted for non business purposes. As noted earlier, the assessee has not advanced any amount

in excess of the amount payable to the H & T contractors under the tripartite agreement. The amount advanced to the H & T contractors is in fact adjusted from the total amount payable by the assessee to the H & T contractors. The amounts that too on interest are advanced to ensure that the H & T contractors supply harvested sugar-cane promptly and efficiently. Once it is held that advancing some amounts to the H & T contractors was in the business interest of the assessee, the question of disallowing proportionate interest on the funds borrowed by the assessee does not arise.

13. As regards the Bakshish (reward) claim of Rs.2,73,000/- is concerned, it is pertinent to note that giving Bakshish to the workers employed by the H & T contractors has been the practice prevailing in the State of Maharashtra for decades and such expenditure has been consistently allowed in the past not only in the case of the assessee but also in the case of several other sugar factories. The Tribunal has noted in the case of Sanjivani (Takli) Sahakari Sakhar Karkhana Ltd. that during the harvesting season which continues during the summer months it becomes difficult for the labourers to work due to adverse climatic conditions. If the H & T contractors labourers leave the work during the harvesting season then the assessee

would suffer immensely till the new labourers are employed. The Tribunal has noted that it is only the skilled labourers who can do the job of harvesting and transporting the sugar-cane and the general labourers cannot do such job work. It is held that with a view to induce the labourers to continue with the work during the summer months, Bakshish ranging from Rs.200/- to Rs.250/- is given to the labourers employed by the H & T contractors. In these circumstances, in our opinion, the finding recorded by the Tribunal that the Bakshish payment is a necessary incidence of the assessee's business cannot be faulted.

14. It is contented by the revenue that during the course of assessment, in spite of repeated requests, the assessee has failed to furnish particulars of the amount given as Bakshish. There is no merit in this contention because, neither in the assessment order nor in this appeal the revenue has doubted the genuineness of the payments of Rs.200/ to Rs.250/- made by the assessee to the labourers employed by the H & T contractors depending upon category of each labourer. According to the assessee, particulars of payment made to each labourer has been filed before the assessing officer and the same has not been doubted. Therefore, where Bakshish payment is not disputed, the fact that the assessee has not submitted its explanation as to

why the said claim should not be rejected cannot be a ground to deny the claim of the assessee. The argument of the revenue that if the Bakshish claim of the assessee is allowed the sugar factories may divert the entire profits by way of Bakshish has no basis, because, wherever it is found that the amounts paid as Bakshish are exorbitant and unreasonable or wholly unconnected to the business, then, in such cases, it will be open to the assessing officer to disallow the claim. However, in the facts of the present case, we are of the opinion, that the Bakshish claim made is reasonable and the said expenditure has been rightly held by the Tribunal allowable as business expenditure.

15. For all the aforesaid reasons, the findings recorded by the Tribunal deserves acceptance. Accordingly, both the questions framed above are answered in favour of the assessee and against the revenue.

16. Appeal is disposed of accordingly with no order as to costs.

(F.I.REBELLO, J.)

(J.P.DEVADHAR, J.)

