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Bombay High Court

IN THE HIGH COURT OF JUDICATURE AT BOMBAY

ORDINARY ORIGINAL CIVIL JURISDICTION

INCOME TAX APPEAL NO.324 OF 2012
WITH
INCOME TAX APPEAL NO.325 OF 2012

M/s Shreenath Motors Pvt.Ltd.
Mumbai 400 053 ...Appellant
v/s
Commissioner of Income Tax-V,
Mumbai 400 020 ...Respondent

Mr S.C. Tiwari with Ms Natasha Mangat for Appellant.
Mr Abhay Ahuja for Respondent.

CORAM : S.C. DHARMADHIKARI &
B.P. COLABAWALLA JJ.

Reserved on : 27th June, 2014.
Pronounced on : 3rd July, 2014.

Oral Judgement [Per B. P. Colabawalla J.] :-

1. These two Appeals under section 260A of the Income Tax Act, 1961 are filed by the Appellant-Assessee against a common order dated 18th November, 2011 (hereinafter referred to as the “impugned order”) passed by the Income Tax Appellate Tribunal, (Mumbai I Bench), (hereinafter referred to as “the ITAT”) in relation to Assessment Years 2005-06 and 2006-07. Since the common questions of facts and law arise in both the Appeals, the

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same have been heard together and are being disposed off by this composite order and judgment.

2. Mr Tiwari, the learned counsel appearing on behalf of the Appellant-Assessee, submitted that in the facts of the present case, a substantial question of law arises in both the appeals and reads as under :-

> *"(A) Whether on the facts and in the circumstances of the case of the appellant and in law the Tribunal has erred in holding that the expenditure on remuneration and training of working Director is not allowable under section 37 of the Income Tax Act 1961 ?"*

3. According to Mr. Tiwari, the ITAT had erred in confirming the disallowance of expenditure on remuneration and training of a working Director of the Appellant-Assessee that was incurred legitimately for the efficient management and conduct of the Appellant-Assessee's business. He submitted that the expenditure was not only legitimate but had a direct nexus with the business of the Appellant-Assessee and was therefore allowable as a deduction under section 37 of the Income Tax Act, 1961. It is in this light that the learned counsel has questioned the correctness of the impugned order of the ITAT.

4. For the sake of convenience, we shall refer to the facts in Income Tax Appeal No.324 of 2012. The brief facts are that for the Assessment Year 2005-06, the Appellant-Assessee filed its return of income declaring a total

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income of Rs.1,31,88,558/- accompanied with the Auditor's Report under section 44AB of the Income Tax Act 1961. This return of income was selected for scrutiny by the Assessing Officer who eventually completed the assessment and passed an Assessment Order dated 31st December, 2007 under section 143(3) of the Act determining the total income at Rs.1,41,67,196/- after making disallowances / additions on various counts. The disallowances for the purposes of the present appeal are Rs.1,75,000/- for fees paid on behalf of Mr. Krishna Kachalia, a Director of the Appellant-Assessee, to S P Jain Institute of Management & Research as well as the salary paid to the said Mr. Krishna Kachalia in the sum of Rs.3,12,500/-.

5. Aggrieved by this assessment order dated 31st December 2007, the Appellant-Assessee preferred an Appeal before the CIT(Appeals) who, after giving an elaborate hearing to the Appellant-Assessee, passed his order on 9th July 2009 partly allowing the Appeal. However, the CIT (Appeals) upheld the disallowances with reference to the amounts of Rs.1,75,000/- and Rs.3,12,500/- respectively.

6. Being dissatisfied with the order of the CIT(Appeals), the Appellant-Assessee filed an Appeal before the ITAT. The main grievance of the Appellant-Assessee against the order of the CIT (Appeals) was upholding the disallowance of the aforesaid sums of Rs.1,75,000/- and Rs.3,12,500/-

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which were incurred by the Appellant-Assessee for training fees and remuneration paid to it's Director, Mr. Krishna Kachalia. These disallowances have been upheld even by the ITAT in the impugned order, and thus the present Appeal.

7. Mr Tiwari submitted that the Appellant-Assessee was looking to grow and expand its business as well as it's marketing needs and for this reason, it sponsored Mr Krishna N. Kachalia, who is the son of another Director of the Appellant-Assessee, Mr Shailesh Kachalia, for an advanced course in marketing with the S.P. Jain Institute of Management & Research. He submitted that the above studies and training of Mr Krishna Kachalia had eventually helped the Appellant-Assessee in it's business since he was independently looking after the VOLVO Division, the dealership of which he was instrumental in acquiring. He submitted that it was only because of Mr Krishna Kachalia that the Appellant-Assessee was able to obtain the distributorship of VOLVO. He further submitted that Mr Krishna Kachalia was stationed at Borivali, looking after Used Car Division as well as the workshop activities and was therefore appointed as a Director of the Appellant-Assessee sometime in 2003 and was paid a salary of Rs3,12,500/-. He submitted that these expenses have a direct nexus with the growth of the business of the Appellant-Assessee and therefore all the authorities below had wrongly disallowed the claim of the Appellant-

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Assessee for the fees paid to S.P. Jain Institute of Management & Research on behalf of Mr Krishna Kachalia as well as the payment of salary to him.

8. On the other hand, Mr Ahuja, the learned counsel appearing on behalf of the Revenue relied upon the observations and findings in the Assessment Order passed under section 143(3) of the Act as well as the order of the Commissioner of Income Tax (Appeals) dated 9th July 2009 to support the the impugned order. He submitted that these Appeals raise no substantial questions of law as the findings given by the Assessing Officer, the CIT (Appeals) as well as the ITAT are all based on the peculiar facts and circumstances of the present case. He submitted that the authorities below, after carefully considering the entire factual matrix have disallowed the aforesaid expenses, and by no stretch of the imagination can it be said that the said findings are perverse or vitiated by an error apparent on the face of the record, and therefore these Appeals have no merit and ought to be dismissed.

9. With the help of the learned counsel for both parties, we have perused the Memo of Appeal and the Annexures thereto as well as the orders passed by the Assessing Officer, CIT(Appeals) and the ITAT. The Assessing officer, in his order dated 31st December, 2007 passed under section 143(3) of the Act found that Mr Krishna Kachalia, who was 26 years old, had completed his graduation in B.Com. in the year 2003 and had been inducted

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as a Director of the Appellant – Assessee on 30th September 2003. After analysing the entire factual matrix, the Assessing Officer came to the conclusion that the said Krishna Kachalia was inducted as a Director at such an early age and immediately after the completion of his B.Com. course only to finance his higher education in Management through the funds of the Appellant-Assessee on which a deduction could be claimed. The Assessing Officer was of the view that the only reason for obtaining such a young person to be a Director who had little or no business experience, was only to claim this deduction and that the payment of fees to S.P. Jain Institute of Management and Research for and on behalf of Mr Krishna Kachalia was out of personal consideration and not out of any commercial consideration. The Assessing Officer further fortified this finding by holding that similar expenditure had not been incurred by the Appellant-Assessee in respect of any other employee not related to the Company's Directors. He therefore proceeded to disallow the Assessee's claim of deduction on the aforesaid count. For identical reasons, the Assessing Officer further went on to disallow the deduction for payment of salary to the said Mr Krishna Kachalia. The Assessing Officer further noted that though Mr Krishna Kachalia was shown to be in-charge of the marketing activity at the Borivali Centre, another Director was also looking after the marketing activities at the very same place and was paid a salary of Rs.10,00,000/- per annum for that work. In no other Centres (Andheri or

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Rajkot) there was more than one Director assigned and therefore the Assessing Officer came to the conclusion that the said Mr Krishna Kachalia was assigned to look after the work at Borivali only in name. Examining the order of the Assessing Officer we do not find that in the peculiar facts and circumstances of the present case the Assessing Officer had, in any way, misdirected himself in coming to the findings that he did. The view taken by the Assessing Officer is not only a possible view, but in our opinion a correct view, requiring no interference.

10. Similarly, the CIT (Appeals) also in paragraph 5.3 of his order dated 9th July 2009 has reaffirmed the findings of the Assessing officer. The CIT(Appeals) came to a finding that it could not be said that the expenditure incurred on the education of Mr Krishna Kachalia who was a Director of the Appellant-Assessee was a legitimate expenditure incurred for the purpose of the business of the Appellant-Assessee, especially in view of the fact that the Appellant-Assessee had not filed any evidence that it had framed any Rules and Regulations for incurring expenditure on education for the son of a Director or any other employee of the Appellant-Assessee. The Appellant-Assessee further had not filed any details which showed that Mr Krishna Kachalia was under any obligation to serve the Appellant-Assessee after completion of his management studies. As far as the salary paid to him as a Director was concerned, the CIT (Appeals) held that Mr Krishna Kachalia

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was doing his management course with S.P. Jain Institute of Management & Research from October 2003 to April 2005 and therefore it was not possible that he was working in the capacity as a Director at the same time when in fact he was a student. In view of these facts, the CIT (Appeals) upheld the findings of the Assessing Officer.

11. The impugned order of the ITAT also makes note of the entire factual matrix and affirms the orders passed by the Assessing Officer as well as the CIT (Appeals) in disallowing the aforesaid claims. The impugned order in fact records that although an attempt was made on behalf of the Appellant-Assessee to make out a case that Mr Krishna Kachalia was instrumental in acquiring distributorship of VOLVO, no evidence whatsoever had been filed to support and substantiate the same. In fact, the ITAT came to a finding that sending Mr. Krishna Kachalia, who was a Commerce Graduate and had joined the Appellant-Assessee just a month back, for a management course in marketing at the cost of the Appellant-Assessee without any exposure or experience, could not be justified on the touchstone of commercial expediency. The ITAT further held that the Appellant-Assessee had not been able to satisfactorily explain the services rendered by Mr Krishna Kachalia and whatever explanation that was sought to be given in this regard was also found to be not acceptable by the Assessing Officer by giving specific reasons. The ITAT holding that the issue in dispute being purely a factual

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one, the onus was on the Appellant-Assessee to establish on evidence that the said expenditures were incurred wholly and exclusively for the purpose of it's business. The Appellant-Assessee having failed to discharge this onus, the findings of the Assessing Officer and the CIT (Appeals) were confirmed.

12. After carefully perusing the orders passed by the authorities below we have no hesitation in holding that the dispute in the present case is purely a factual one. We find that the facts and the evidence brought on record by the Appellant-Assessee have been analysed by all the authorities below and in it's proper perspective. In this view of the matter and in the peculiar facts of the present case and noting the findings given by the ITAT which are based on the facts and circumstances of the case, we are not required to decide any larger question in these Appeals. We find that the dispute in the present case being purely of a factual nature, does not raise any substantial question of law and the orders passed by the authorities below can in no way be said to be vitiated on the ground of perversity or any error apparent on the face of the record.

13. The reliance placed by Mr. Tiwari on a Division Bench judgment of this Court in the case of ***Sakal Papers Pvt.Ltd. v/s Commissioner of Income Tax, reported in (1978) 114 ITR 256 (Bom)*** is wholly misplaced.

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In the facts of that case, this Court found that Ms Leela Parulekar, a daughter of the two Directors of the Assessee Company had gone to USA for education after completing her Masters of Arts from Poona University. The Assessee Company was in the business of publishing a leading Marathi daily newspaper in Poona. Ms Leela Parulekar worked in the Editorial Department of the newspaper from September 1955, starting as an apprentice, on a salary of Rs.50/- p.m. and on 24th March 1960 (i.e. after 5 years), the Directors of the Company passed a resolution that the said Ms Leela Parulekar should be sent for specialised education in journalism and business administration in a university of good standing in U.S.A. which the Directors believed would be good for the progress of the paper. On these facts, this Court found that (i) prior to her being selected, the said Ms Leela Parulekar had for five years worked for the paper starting as an apprentice; (ii) the selection of Ms Leela Parulekar was proper, and that her training would be of assistance to the Assessee Company; (iii) she attended the Graduates' School of Journalism at Columbia University in New York, secured a degree of Masters in Journalism and thereafter spent three months obtaining practical training in printing and lithography; and (iv) on her return from U.S.A., the said Ms Leela Parulekar once again joined the Editorial Board of the Company and was still working with the Company. It is on these facts that this Court came to the conclusion that merely because there was no commitment or contract or bond taken from the trainee, the

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expenditure, which was otherwise proper, should not be disallowed to the Assessee Company, particularly when as a result of that expenditure, the trainee had secured a degree and training which would be of assistance and was in fact of assistance to the Assessee Company after her return to India.

14. We find that the facts in the present case as narrated earlier in this judgement are totally different. In the present case, the authorities have found that the expenditure incurred for the education of the Director of the Appellant-Assessee viz. Mr Krishna Kachalia was out of personal consideration and not commercial consideration. The authorities below, being fact finding authorities, have come to the aforesaid conclusion after taking into consideration the totality of the facts and circumstances of the case. We find the said findings in consonance with the facts and circumstances of the present case. Furthermore, the judgement in *Sakal Papers Pvt. Ltd. (supra)* has been considered by another Division Bench of this Court in ***Income Tax Appeal No.840 of 2012 in the case of D.C. Mehta v/s The Income Tax Officer 11(2)(2) and anr., dated 11th March 2014***. The reliance placed by Mr. Ahuja on the judgement in the case of *D. C. Mehta (supra)* is well founded. In the facts of that case, the Assessee, Mr. D. C. Mehta, was a Advocate by profession. In the return of income filed by the Assessee, the Assessing Officer noticed a deduction of Rs.22,25,614/- claimed by the Assessee as expenditure incurred for higher education for his

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daughter, Hemali. The justification for the said deduction was that she joined the Appellant's firm of Advocates and gave an undertaking that on attaining higher qualification and degree from the University abroad, she would join the firm for a minimum period of five years and thus, the said expenditure was incurred for the business of the Assessee and was allowable as a deduction. This Court had the occasion to consider the judgment in the case of *Sakal Papers Pvt.Ltd. (supra)* when it held that the facts were different and distinct from the facts in *Sakal Papers Pvt.Ltd.'s case*. It was found that the daughter Hemali joined the Assessee and immediately was sent for education abroad. The Assessee had not been able to bring on record anything and particularly the scheme for higher education abroad for employees and associates. Despite other associate Advocates working in the firm of the Assessee, none were given an opportunity to go abroad for higher education despite the fact that some were working with him for the last 15 years. Despite the aforesaid, within a period of two to three months, after the daughter Hemali became an Advocate and joined the firm as an Associate, she went abroad. In this view of the matter, the Division Bench of this Court upheld the contention of the authorities below in disallowing the deduction of Rs.22,25,614/- incurred by the Assessee for the higher education of his daughter, Hemali. The Division Bench in *D. C. Mehta's case (supra)* in paragraph 5 of the judgment has specifically stated that the judgment in *Sakal Papers Pvt.Ltd.'s case* must be seen in the

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peculiar facts and background. After analysing the facts in the case of *Sakal Papers Pvt.Ltd. (supra)*, the Division Bench *in D. C. Mehta's case (supra)* held that the cumulative impact of all the events & circumstances in the case of *Sakal Papers Pvt. Ltd. (supra)* led this Court to hold that the deduction could not have been disallowed. It is in these circumstances, this Court in *Sakal Papers Pvt.Ltd.'s case* has held that only because there was no commitment or contract or bond taken from the trainee, the expenditure cannot be disallowed to the Assessee, particularly when as a result of that expenditure, the trainee had secured both, a degree and training which would be of assistance to the Assessee Company. We find that the facts of the present case are totally different from that in the case of *Sakal papers Pvt. Ltd.* and almost identical to that in *D. C. Mehta's case*. In the case of *D. C. Mehta (supra)* this court did not interfere with the findings of the authorities below in disallowing the deduction to the Assessee. In this view of the matter, we find that the reliance placed by Mr. Tiwari on the judgment of this Court in the case of *Sakal Papers Pvt.Ltd. (supra)* is wholly misplaced.

15. Similarly, we also find that the reliance placed by Mr Tiwari on the judgments of the supreme Court in the case of ***Commissioner of Income Tax v/s Chandulal Keshavlal and Co., reported in (1960) 38 ITR 601*** and in the case of ***S.A. Builders Ltd. v/s Commissioner of Income Tax (Appeals) and anr., reported in (2007) 288 ITR 1*** are also of no assistance.

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In the case of *Chandulal Keshavlal and Co. (supra)*, the Supreme Court held as under :-

> *"The cases we have discussed above show that it is a question of fact in each case whether the amount which is claimed as a deductible allowance under s. 10(2)(xv) of the IT Act was laid out wholly and exclusively for the purpose of such business and if the fact finding tribunal comes to the conclusion on evidence which would justify that conclusion it being for them to find the evidence and to give the finding then it will become an admissible deduction. The decision of such questions is for the Tribunal and the decision must be sustained if there is evidence upon which the Tribunal could have arrived at such a conclusion.*
>
> *Another fact that emerges from these cases is that if the expense is incurred for fostering the business of another only or was made by way of distribution of profits or was wholly gratuitous or for some improper or oblique purpose outside the course of business then the expense is not deductible. In deciding whether a payment of money is a deductible expenditure one has to take into consideration questions of commercial expediency and the principles of ordinary commercial trading."*
>
> (emphasis supplied).

16. Similarly, in the case of S.A. Builders Ltd. (supra), the Supreme Court has held as under :-

> *"31. We agree with the view taken by the Delhi High Court in CIT vs. Dalmia Cement (Bharat) Ltd. (2002) 174 CTR (Del) 188 : (2002) 254 ITR 377 (Del) that once it is established that there was nexus between the expenditure and the purpose of the business (which need not necessarily be the business of the assessee itself), the Revenue cannot justifiably claim to put itself in the armchair of the businessman or in the position of the board of directors and assume the role to decide how much is reasonable expenditure having regard to the circumstances of the case. No businessman can be compelled to maximize its profit. The IT authorities must put themselves in the shoes of the assessee and see how a prudent businessman would act. The authorities must not look at the matter from their own viewpoint but that of a prudent businessman. As already stated above, we have to see the transfer of the borrowed funds to a sister-concern from the point of view of commercial expediency ant not from the point of view whether the amount was advanced for earning profits."*
>
> (emphasis supplied).

16. What can be discerned from the aforesaid Supreme Court judgments is that (a) the amount which is claimed as a deductible allowance

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was wholly and exclusively for the purpose of the business of the Assessee; (b) there has to be a nexus between the expenditure incurred and the purpose of the business; and (c) these are all questions of fact that have to be determined by the authorities below. If the fact finding Tribunal comes to the conclusion on evidence, that would justify allowing the deduction, then it would become an admissible deduction. The decisions on such questions is for the Tribunal to decide and the decision must be sustained if there is evidence upon which the Tribunal could have arrived at such a conclusion. However, as reiterated by the Supreme Court, this would depend on the facts and circumstances of each case. In the present case, we find that the reliance placed on the aforesaid judgments is of no assistance to the Appellant-Assessee. In the facts of the present case, the authorities below have come to a categorical finding (i) that the expenditure incurred was not for the purpose of business of the Appellant-Assessee and was out of personal consideration and not out of any commercial consideration; (ii) that the Appellant-Assessee filed no evidence that it had framed any Rules or Regulations for incurring expenditure on the education of the son of the director or any other employee; (iii) that the Appellant-Assessee had not filed any details which would indicate that the said Mr Krishna Kachalia was under any obligation to serve the Appellant-Assessee after the completion of management studies; (iv) that the Appellant-Assessee had paid education expenses of Mr Krishna Kachalia only because he happens to

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be belonging to the family controlling the Appellant-Assessee; (v) that the expenditure incurred on the education of Mr Krishna Kachalia was not incurred for the purpose of business of the Appellant-Assessee and therefore could not be allowed as deduction in the hands of the Appellant. In view of these categorical findings of fact, we have no hesitation in holding that the deduction claimed by the Appellant-Assessee has been rightly disallowed by the authorities below and we find no infirmity in the impugned order passed by the ITAT.

17. On the same parity of reasoning, we find that even the expenses claimed as a deduction by the Appellant-Assessee for the payment of salary to Mr Krishna Kachalia was rightly disallowed by the authorities below. In this regard, the authorities below have come to a finding that the said Mr Krishna Kachalia was doing a management course with S.P. Jain Institute of Management & Research from October 2003 to April 2005 and therefore it was not possible that he was working for the company in the capacity of a Director at the same time when in fact he was a student. The authorities below have come to a finding that during the time Mr Krishna Kachalia was shown to be in-charge of the marketing activities at the Appellant-Assessee's Borivali Center, another Director of the Appellant-Assessee was also looking after the marketing activities at the very same place and was paid a remuneration of Rs.10,00,000/- per annum for the said work. The

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authorities below have also found that in no other Center of the Appellant-Assessee was more than one Director assigned and the fact that Mr Krishna Kachalia was assigned to look after the work at Borivali in addition to another Director, his appointment was only for name sake. Despite the fact that it was sought to be urged that Mr Krishna Kachalia was rendering marketing services to the Assessee Company in the year under consideration and that he was instrumental in acquiring the distributorship of VOLVO and thereafter dealing with such distributorship, no evidence was led by the Appellant-Assessee to support and substantiate the same. We therefore find that even on this count the authorities below were fully justified in disallowing the said deduction.

18. In view of the aforesaid facts, we find that these Appeals do not raise any substantial question of law, the impugned order does not require any interference and therefore, the Appeals are dismissed.

19. In the facts and circumstances of the case, the Appellant-Assessee shall pay costs of Rs.50,000/- to the Respondents.

(B.P. COLABAWALLA J.) **(S.C. DHARMADHIKARI J.)**

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