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IN THE HIGH COURT OF JUDICATURE AT BOMBAY
ORDINARY ORIGINAL CIVIL JURISDICTION

INCOME TAX APPEAL NO.1376 OF 2000 (AY 1991-92)
WITH
INCOME TAX APPEAL NO.1378 OF 2000 (AY 1993-94)
WITH
INCOME TAX APPEAL NO.1379 OF 2000 (AY 1992-93)

M/s. T. Lakhamshi Ladha & Co.

..Appellant

Versus

The Commissioner of Income Tax

..Respondent

.....

Mr. Nitesh Joshi i/b. S. R. Rawell & Co. for the Applicant.

Mr. Suresh Kumar a/w Ms. Samiksha Kanani for the Respondent.

.....

CORAM: M. S. SANKLECHA &
A. K. MENON, JJ.

RESERVED ON : 7TH APRIL, 2016

PRONOUNCED ON : 4TH MAY 2016

Judgment (Per. A.K.Menon J.)

1. These three Appeals under Section 260A of the Income Tax Act 1960 ("the Act") were admitted on 26th February 2002 in respect of assessment years 1991-92, 1992-93 and 1993-94. All three appeals were admitted on an identical substantial question of law save and except that the amounts in dispute as indicated in the questions in the three appeals are

different. For the purpose of these appeals this Court re-framed the solitary substantial question of law excluding the amounts in respect of each assessment year :-

Whether on facts and the circumstances of the case, Tribunal was right in sustaining the addition made on account of payment of "Mehta Sukhadi" ?

Facts .

2. As the facts are similar in all three appeals we shall refer to the facts set out in Income Tax Appeal No.1376 of 2000 relating to A.Y. 1991-92.

(a) The appellant is a partnership firm engaged in the business of letting on hire tarpaulin sheets for the purposes of erecting weather sheds. The appellant has numerous clients who have engaged the appellant for providing tarpaulin sheets for putting up protective weather sheds. It is the appellant's case that in the regular course of their business they are required to incur and pay costs by way of secret commission allegedly known in the trade as "*Mehta Sukhadi*". According to the appellant, such commission has been paid secretly to employees of numerous clients and those amounts are deductible under Section 37(1) of the Income Tax Act, 1961 (the Act) as business expenditure.

3. In respect of A.Y. 1991-92 the assessee filed its return of income on 30th October, 1991 declaring income of Rs. 8.66 lakhs. In its return of income the appellant had debited an amount of Rs.1.45 lakhs as "Mehta Sukhadi" i.e. secret commission paid to employees of its customers. The Assessing Officer by his order dated 31st March 1992 passed under Section 143(3) of the Act disallowed the secret commission by relying upon his Order in the Appellants case for A.Y. 1990-91. Our attention was invited to the order dated 31.3.1992 passed by the Assessing Officer for AY 1990-91 wherein also the appellant claimed payment of secret commission to the employees of companies to whom tarpaulins were given on rent. In Assessment year 1990-91 this amounted to Rs.1,37,375/-. In respect of this alleged payment of secret commission there were no receipts or vouchers or any other written evidence. The assessee's representative submitted before the Assessing Officer that on account of severe competition they were required to make certain percentage of the contract amount to select employees of clients, secretly, in order to approve the assessee's contracts, rates and help in getting quick payment of such hire charges. According to the appellants, these amounts are allowable as business expenditure. The representative submitted that it is not possible to disclose the names of employees to whom payments of secret commission were made. These payments are allegedly made in cash. The Assessing

Officer recorded in the Assessment Order that all payments were allegedly made in cash and a list of companies from whom the payments were received during the year along with details of payments made to employees of the said companies had been furnished by the Appellant. This amounted to 1% and 3% of the receipts.

4. The assessee relied upon the decisions in *Commissioner of Income Tax Vs. Sigma Paints Ltd. 188 ITR 6, Commissioner of Income Tax Vs. Goodlass Nerolac Paints Ltd. 188 ITR 1* as also the unreported decision of the Special Bench of the Tribunal in *First Income Tax Officer Vs. French Dyes & Chemicals (I) Pvt. Ltd. (Income Tax Appeals Nos.182 to 194 of 1982 dated 31st July, 1984)*. The appellants contended that in aforesaid cases, payments were made to employees of various companies and just like in the appellants case, names and addresses of the recipients were not furnished. In the present case the Assessing Officer declined to grant any relief to the assessee, observing inter alia that in the precedents cited, secret commission paid was less than ½% of the turnover, whereas in the case of the appellant-assessee the percentage was between 1% to 3% averaging to 2.5% which was held to be unreasonable. The Assessing Officer disallowed the entire deduction claimed by way of payment of secret commission.

5. Being aggrieved, an appeal was filed before the Commissioner of Income Tax (Appeals). By an order dated 26th February, 1993 the Commissioner of Income Tax (Appeals) reversed the order of the Assessing Officer observing that the payments were in the nature of liaison charges and secret commission.

6. Aggrieved, the Revenue appealed to the Tribunal which questioned the deletion of the addition on account of Secret Commission on the basis that the Commissioner of Income Tax (Appeals) did not appreciate this Court's decision in the case of Goodlass Nerolac Paints Ltd.,(supra) and the Supreme Court's decision in the case of **CIT Vs.**

Gannon Dunkerley & Co. Ltd. 167 ITR 637 which held that the issue of secret commission is one of law and not fact. The Revenue was in appeal for orders of the Commissioner of Income-Tax (Appeal) relating to A.Y. 1989-90, 1990-91, 1991-92 and 1993-94. The Tribunal heard appeals relating to all the above years together and passed a common impugned order on 31st January, 2000. It held that the appellants was given an opportunity by the Assessing Officer to substantiate the claim but the appellant simply contended that in their line of business, due to severe competition, a percentage of receivables had to be paid to select employee(s) secretly

and which amounts were deductible as business expenses.

7. The Tribunal concluded that the assessee had failed to provide documentary evidence to substantiate the payment of secret commission. It also recorded that the appellant was unable to give names of recipients of the commission. Thus reversed the order of the Commissioner of Income Tax (Appeals). In doing so the Tribunal did not rely solely on the fact that the appellant had not furnished the names of recipients of the commission but held that evidence adduced was not enough to substantiate the actual payment of commission. The assessee-appellant is before us being aggrieved by the order of the Tribunal.

Submissions on behalf the Assessee.

8. Mr. Joshi, the learned counsel appearing on behalf of the appellants has taken us through the various factual aspects. He made three submissions. Firstly he submitted that there was sufficient evidence before the Assessing Officer to support the order passed by the Commissioner of Income Tax (Appeals). The Assessing officer had failed to appreciate that being secret commission by its very nature the names of recipients could not be disclosed. The CIT (Appeals) had appreciated the evidence and held in his favour.

9. Secondly, he submitted that there were several documents filed before the Tribunal which were not referred to in the order passed by the Tribunal. The Tribunal could not have upturned the CIT(Appeals) finding without spelling out the deficiencies in evidence led by the assessee. Mr. Joshi contended that the appellants had filed two compilations of documents containing evidence of Mehta Sukhadi (secret commission) paid which, according to him, were available before the Commissioner of Income Tax (Appeals) and the Tribunal. However, the Tribunal has erroneously concluded that no evidence was available in respect of the secret commission paid. Based on the references made in the Order of the CIT Appeals, we permitted the appellants to rely upon the following documents which were before the CIT (Appeals):-

- (a) Copy of list of Mehta Sukhadi paid from A.Y. 1978-79 to 1991-92.
- (b) Copy of statement giving client names, amounts received and amounts paid as Mehta Sukhadi.

10. Mr. Joshi submitted that reference to these documents would reveal that the

appellants had furnished a statement in which the particulars of secret commission was detailed. One of the documents relied upon before the CIT(Appeals) is a list showing secret commission allegedly paid over 10 to 15 years against gross hire charges. This list discloses that between 1990-91 and 2003 diverse amounts have been paid as secret commission ranging between 2.2% to 2.37%. Similar statements have been filed for the year 1989-90, 1991-92, 1988-89 and 1987-88.

11. Thirdly, Mr. Joshi, submitted that the Tribunal had not spelt out as to why it chose to discard the reliance placed by the CIT (Appeals) upon a typed statement of Mehta Sukhadi allegedly paid during the year 1990-91 in respect of diverse clients.

12. Based on the aforesaid documents which were admittedly available before the CIT (Appeals), the CIT (Appeals) accepted the same as sufficient evidence and permitted deduction. Mr. Joshi thereafter took us through various decisions of this Court, firstly, Mr. Joshi sought to rely upon the fact that secret commission had been recognized in the pronouncement in Goodlass (Supra). In paragraph 5 of the said judgment it is recorded that in order to be entitled to deduction of payments to persons whose name were not disclosed, the assessee has to establish the practice

prevailing in that line of business for making such payments. It has to adduce evidence to establish the payments and has to satisfy the authorities that the payments were in fact made for the purpose of business.

13. Mr. Joshi then relied upon the decisions of this Court in the matter of Sigma Paints Ltd. (supra), and submitted that the tribunal had found that there was sufficient evidence to support the case of payment of secret commission. Relying upon the decision of the Hon'ble Supreme Court in the Gannon Dunkerley and Co. Ltd. (supra), Mr. Joshi submitted that the Hon'ble Supreme Court had held that the question of deduction of secret commission was question of law and had directed the question to be referred to the High Court for its opinion.

14. Mr. Joshi then relied upon the judgment of the Orissa High Court in **Tarini Tarpauline Productions Vs. Commissioner of Income Tax** 254 ITR Page 495 wherein the effect of amendment of explanation to Section 37(1) came to be considered. In the present case Mr. Joshi submitted that the payment of secret commission is not illegal inasmuch as offering commission to private party is not an offence. In the context of explanation to Section 37(I), it may be offence to offer such

payment to Government officers/authorities but this did not in any way affect the assessee's payment by way of secret commission in the case at hand.

15. Mr.Joshi then relied upon decision of this Court in **Commissioner of Income Tax vs. Gill and Co. Pvt. Ltd. 248 ITR Page 362** and submitted that the Appellate Authority and Tribunal in that case had proceeded to allow the claim for deduction in respect of secret commission as it was observed that claims in past were also allowed. In yet another case relied upon by Mr.Joshi of **Dr.G.G.Joshi vs. Commissioner of Income Tax (1994) 209 ITR Page 324** wherein Gujarat High Court had occasion to consider payment of secret commission and the High Court found that the Tribunal was satisfied that payment of secret commission was established as a practice prevailing in that line of business and the tribunal having come to such a finding, the same cannot be interfered with by the High Court. According to Mr.Joshi the facts in the present case are eminently in line with the facts in other cases where secret commission has been allowed, therefore, he submitted that in the present case also that commission ought not to be denied.

16. Mr.Joshi then relied upon the case of Gannon Dunkerley (supra) wherein it was held that secret commission paid by the assessee to procure business was not deductible as a result of amendment to Section 37(1). According to Mr.Joshi private parties were not prohibited from offering secret commission and such payment did not militate against provisions of Section 37(I) including the explanation. In this view of the matter Mr.Joshi submitted that the appellants were well within their rights to claim a deduction.

Submissions on behalf the Revenue .

17. Mr.Suresh Kumar Learned Counsel appearing for the revenue submitted that the payment of secret commission could not be allowed as deduction. According to Mr.Suresh Kumar, in the present case, there was no evidence whatsoever to support the petitioner's case and the judgments referred to by Mr.Joshi cannot come to his assistance since there was no evidence that payments were in fact made and that these payments were made for the purpose of business of the assessee.

18. Mr.Suresh Kumar relied upon the decision of the Tribunal in the case of I.T.O V/s. D.B. Taraporevala Sons & Co. 2005(1) SOT 123(Mum) in which it is held that the assessee was given many opportunities to bring out details with regard to

expenditure claimed but they failed to do so. It was stated that when the assessee claims such expenditure as deductions, the burden of proving that such expenditure was incurred is entirely upon the assessee and which included the burden of proving that the expenditure that was incurred for the purpose of business and if the same is not proved it may be presumed that it was not so incurred. In the instant case the assessee did not produce evidence that the payment was actually made and did not discharge that burden.

19. Mr.Suresh Kumar relied upon observation in case of the CIT vs. Gill and Co. (supra) wherein it was held that merely because the orders are passed in favour of the assessee in earlier years it cannot be a ground to allow deduction in subsequent years specially after amendment to Section 37(1) and introduction of the explanation. Mr.Suresh Kumar then relied upon the decision of this Court in case of **Harish Textile Engrs. Ltd. vs. DCIT (2015) 379 ITR 160** to which one of us (M.S. Sanklecha, J) was a party and in which case the appeal had been admitted and the substantial question of law involved consideration of 'on money' received by a party. This Court had held that in the absence of evidence in the form of any entry in books of accounts or other documents to show receipt of money by the appellant, the

amount added to the appellant's income as "on money" received was unsustainable in law. That in a subsequent period there was evidence available as to receipt of "on money". However, for the period in question the addition was deleted for want of evidence.

20. He then relied upon the decision of the Punjab and Haryana High Court in ***CIT, Jalandhar vs. Dhanpat Rai & Sons 42 Taxmann 475*** in support of his submission that any secret payment that is made to secure an unfair advantage would necessarily be repugnant to law. Such transactions are not transparent, offends normal business practice and such unexplained and unvouched expenditure if allowed would encourage illegal payments, evasion of tax and unscrupulous practices ushering in at both ends. Mr.Suresh Kumar relied upon the finding that the expenditure incurred on secret commission would necessarily fall within the mischief of the explanation added to Section 37(1) of the Act. Mr.Suresh Kumar submitted that in the present case also there is no evidence to establish the claim of the appellant. The fact situation in the instant case according to Mr.Suresh Kumar does not warrant interference since it has not been established that payments of secret commission were in fact made by the assessee.

Consideration.

21. We have heard both sides at length and counsel have ably assisted us. The Assessing officer held that although it was the appellants case that payment of secret commission ensured quick payment of hire charges, the particulars in the instant case revealed that hire charges running into lakhs of rupees remained overdue and that the payment of secret commission even if correct cannot be justified. The Assessing Officer dealt with various other aspects of cash amounting to Rs.2,72,980/- found and seized as unaccounted and various blank signed debit cash vouchers found in order to inflate labour charges which do not concern us in the present appeals which only pertain to the payment of secret commission.

22. The order of the first appellate authority reveals that the partners of the appellants were stated to be present before the Commissioner of Income Tax (Appeals) and they reportedly confirmed that the disbursements were made the partners in charge of the particular client's site by withdrawing money from bank. The Commissioner of Income Tax (Appeals) further observed that the Assessing Officer had noted that the appellant had furnished details of payment but the names of recipients were not made available. In paragraph 17 of the order of the Commissioner

of Income Tax (Appeals) had observed that on perusal of the details and the decisions relied upon by the appellant, they have rendered a proper account of payment received from various companies and the amount of secret commission paid by the assessee to the staff of such companies. The only detail missing was the names of recipients. The Commissioner of Income Tax (Appeals) recorded that the appellant has been following this procedure for last 30 years and the details furnished show that payments are neither were large payments made to any single company nor were the payments out of the way. The CIT (Appeals) concluded that the details submitted before him established that the rate of secret commission at 2.5% is reasonable and following the decision of this Court in Goodlass Nerolac Paints Ltd. (supra) the appellants contentions were accepted and the addition made on account of Mehta Sukhadi were deleted.

23. Although Mr.Joshi sought to contend that further documents were available, we declined to entertain this contention as we would not be justified in allowing Mr.Joshi to rely upon other disputed documents at this stage particularly when the same is not a part of the record before us. We noticed that during the arguments leading to the impugned order before the Tribunal the appellant had placed reliance

on the decision of the Tribunal in case of M/s. French Dyes and Chemicals India Pvt. Ltd. Vs. Commissioner of Income-Tax (unreported). However the aforesaid decision was not available for our perusal. However we were informed by Mr.Suresh Kumar that the assessee M/s. French Dyes and Chemicals India Pvt. Ltd. had filed an SLP and the Civil Appeal which came to be decided on 18th February, 1993 reported in 1993 (Supp.) 3 SCC 195 wherein the Supreme Court heard a challenge against the judgment of Bombay High Court refusing to frame a question of law. From a perusal of the tribunal's judgment in French Dyes (supra) it was found that the assessee had failed to establish that the said amount was expended for the purpose indicated by the assessee. The finding was based on more than one circumstance. The Supreme Court observed that not only had the assessee failed to disclose names of recipients but even the commission allegedly paid was not uniform.

25. It was further pointed out that the mere fact that certain amounts were made available to the Director of the assessee was not sufficient proof of its payment, inasmuch as, according to the assessee, the amounts were not paid by the Director by himself but through various employees. The names of persons who had allegedly

made payments to the Dyeing Masters of the clients had also not been disclosed. In this view of the matter the tribunal recorded the finding that the assessee therein had failed to establish that the said expenditure was incurred.

26. In the case of Goodlass Nerolac (supra) the Tribunal had considered the facts and found that the assessee was maintaining proper accounts and records with regard to the payments and that the payments were made under the instructions and directions of the top executives of the company and were approved by the Board of Directors at the end of every month. The Tribunal found in the facts of Goodlass Nerolac (supra) that the assessee was a public limited company whose accounts were not merely audited but were also placed before the general body of the shareholders. Moreover the assessee's turnover in Goodlas Nerolac (supra) was increasing year after year whereas amounts claimed as eligible for deduction had dropped from 1.34% to 0.22% in the year in question. These were considered to be very relevant and on the basis of this and other evidence the Tribunal concluded that the fact of payment of commission had been established in the case of Goodlas Nerolac (supra) even though the names and addresses of the recipient were not provided. It was

further found by the tribunal that the payments were made for the purpose of business. Relying on this decision Mr.Joshi alluded to the present fact situation and submitted that in the circumstances the assessee should be held to have proved these payments and that these payments accordingly qualified for deduction.

27. In Sigma Paints (supra) the assessee had maintained a record of payment of secret commission including vouchers for the amounts received by the sales officer and other responsible person for the payment of secret commission. The details of sales transaction entered into with various companies, in respect of which secret commission had to be paid, were available. There was complete tally between the commission paid and the extent of business done by the company. Details of the exact transactions in respect of which the assessee had paid secret commission, were also available. The assessee had given a complete list showing the turnover and the amount of secret commission paid from year to to year. The percentage of secret commission was minimal. All details of payment on the above basis in respect of several parties were available. The only missing item was stated to be the names of the particular parties to whom the payments were made. The Tribunal held that these names could not be supplied without detriment to the business of the assessee and in

the very nature of things it was not possible to expect the assessee to reveal these names.

28. In Gannon Dunkerley (supra) the question “Whether, on the facts and in the circumstances of the case, the tribunal was right in holding that the expenditure by way of secret commission was deductible under Section 37(1) of the Act in computing the business income of the assessee ?” was held to be a question of law and the High Court was required to answer it.

29. In Tarini Tarpauline (supra) it was found that an explanation had been added to Section 37(1) of the Act with effect from 1st April, 1992 and it was declared that any expenditure incurred by an assessee for any purpose which is an offence or which is prohibited by law shall not be deemed to have been incurred for the purpose of business or provision and no deduction or allowance shall be made in respect of such expenditure. In that case, the court found merit in the submission of the counsel for the revenue that in view of amendment to Section 37(I) of the Act with retrospective effect the matter required reconsideration and the Tribunal was directed to decide the issue in the light of explanation inserted in Section 37(I).

30. In Gill & Co (supra) since the explanation to Section 37(I) had not been introduced to the statute book it was held that such reliance could not have been placed on the orders passed in favour of the assessee in past the issue came to be remanded back to the tribunal. In Dr. G.G. Joshi (supra) the secret commission was held to be deductible in that case. It was observed that since the assessee had established that the practice of paying secret commission was prevailing in that line of business and the evidence established that payments had been made for the purpose of business.

31. In Gannon Dunkerley (supra) also the assessee was not inclined to disclose the identity of persons to whom commission was paid. The Assessing Officer did not accept the claim that the payments was made for the purpose of business. The assessee appeared before the CIT (Appeals) without success, yet again the made second appeal to the Tribunal but without success. The High Court then answered the question in favour of revenue and against the assessee specially in view of amendment.

32. We find that the facts of the present case are closest to the facts in the

case of French Dyes (supra) as evidenced from the Apex Court order that although the CIT (Appeals) had reached a finding that there was some evidence on record which justified payments to qualify for deduction, the tribunal found that there was no evidence to justify the allowance of deduction. The Assessing Officer also had at the material time found the evidence lacking. The CIT (Appeals) appeared to be satisfied with the evidence but the tribunal was dissatisfied with the evidence. When we examined the order of CIT(Appeals) in the case at hand, we find that evidence relied upon by CIT (Appeals) is not dealt with at all in the satisfactory manner. Vague references are made to the statement made by the partners of the assessee firm whose presence had been recorded by CIT (Appeals) at the hearing. The CIT (Appeals) does not record any substantial evidence that had been provided and except to say that some documentary evidence was produced, the order of CIT (Appeals) leaves much to be desired and fails to inspire confidence. Apart from the fact that the names of recipients are not mentioned, we do not find any attempt on the part of assessee to lead any evidence indicating how these payments were made. None of the partners have given evidence to establish as to which partners dealt with various clients, whose names were not provided in the list forming part of the record. Although the list, a copy of which is now been taken on record, pursuant to

the order in Notice of Motion reveals names of clients, most of whom are corporates, the assessee made no attempt to adduce any evidence as to which the partners dealt with clients in question. No attempt has been made to establish whether the payments were for the purpose of business. In fact the Assessing Officer has in our view rightly concluded that payment of commission did not result in any expeditious payments due to the assessee. Moreover, the finding of fact reveal that the rate of commission was not uniform. There is no evidence brought on record by the appellant to establish that payment of commission was matter of trade practice in its line of business. In absence of such evidence, we are inclined to accept the findings of the tribunal which is last fact finding authority and as such we are not inclined to interfere with this finding.

33. In the view we have taken on the basis of the law existing at the time, the impugned order was passed to hold that the appellant had not established the payment of secret commission. No occasion arises to examine the application of the Explanation 1 to Section 37 of the Act, which would arise only if it is held that the expenditure of secret commission had in fact been incurred of the purposes of business.

34. In the result, the appeal must fail and the substantial question of law raised for our consideration in all the three appeals viz **“Whether on facts and the circumstances of the case, Tribunal was right in sustaining the addition made on account of payment of “Mehta Sukhadi” ?** is answered in the affirmative i.e. in favour of the revenue and against the assessee. All three Appeals disposed off accordingly. There will be no order as to costs.

(A. K. MENON, J.)

(M. S. SANKLECHA, J.)

Wadhwa