

1953

April 17.

COMMISSIONER OF INCOME-TAX,
WEST BENGAL

v.

H. HIRJEE.

[PATANJALI SASTRI C.J., MUKHERJEA, S. R. DAS
and GHULAM HASAN JJ.]*Indian Income-tax Act (XI of 1922), s. 10 (2) (xv)—Business expenditure—Expenses incurred by businessman in defending against criminal prosecution for offence under Hoarding and Profiteering Act—Finding of fact—When final.*

The respondent who carried on business was prosecuted under s. 13 of the Hoarding and Profiteering Ordinance of 1943 on a charge of selling goods at an unreasonable price. He was finally acquitted and claimed in his assessment for a subsequent year that the sum of Rs. 10,895 which he had spent in defending himself against the charge should be deducted from his income under s. 10(2)(xv) of the Income-tax Act as "expenditure laid out or expended wholly and exclusively for purposes of the business". The Appellate Tribunal held that in the absence of any evidence that personal liberty was likely to be jeopardised there was only a chance of his being fined, that the object of saving himself from fine was so inextricably mixed with the main purpose of the defence which was solely for the purpose of maintaining the respondent's name as a good businessman and also to save his stock from being undersold, that it could be ignored, and that, therefore, the claim was allowable under s. 10(2)(xv). On a reference the High Court held that the finding of the Tribunal was one of fact and was binding on it. On further appeal: *Held* (i) that the finding of the Tribunal was not one of fact and was not decisive of the reference; (ii) the finding of the Tribunal was vitiated by its refusal to consider the possibility of the prosecution ending in a sentence of imprisonment and throwing on the Income-tax authorities the burden to prove that the prosecution might result in his imprisonment; and the finding was not therefore binding on the Court; (iii) in any event, the expenses could not be said to be "expenditure laid out or expended wholly and exclusively for the purposes of the business" within s. 10(2)(xv) of the Act.

Legal expenses incurred in civil litigation arising out of matters incidental to the carrying on of a business stand on a different footing as in such a case no question could arise as to the primary or secondary purpose for which the expenses could be said to have been incurred.

The deductibility of such expenses under s. 10 (2) (xv) must depend on the nature and purpose of the legal proceeding and not

on the final outcome of it and a distinction cannot therefore be drawn between expenses of a successful and unsuccessful defence for purposes of s. 10 (2) (xv).

J. B. Advani v. Commissioner of Income-tax ([1950] 18 I.T.R. 557) referred to. *Commissioner of Income-tax v. Maharajadhiraj of Darbhanga* ([1942] L. R. 69 I.A. 15) distinguished.

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CIVIL APPELLATE JURISDICTION: Civil Appeal No. 75 of 1952.

Appeal from the Judgment and Order dated the 16th January, 1951, of the High Court of Judicature at Calcutta (Harries C.J. and Banerjee J.) in Income-tax Reference No. 46 of 1950.

C. K. Daphtary, Solicitor-General for India (G. N. Joshi, with him) for the appellant.

N. C. Chatterjee (P. K. Sen Gupta, with him) for the respondent.

1953. April 17. The Judgment of the Court was delivered by

PATANJALI SASTRI C.J.—This is an appeal from a judgment of the High Court of Judicature at Calcutta answering a reference under section 66-A of the Indian Income-tax Act, 1922 (hereinafter referred to as the Act) in favour of the respondent herein.

The respondent carries on business as selling agents of the Bengal Potteries Ltd., and he was prosecuted under section 13 of the Hoarding and Profiteering Ordinance, 1943, (Ordinance No. XXXV of 1943) on a charge of selling goods at prices higher than were reasonable in contravention of the provisions of section 6 thereof. It appears that before the prosecution was launched in August, 1944, respondent's business premises were searched and a part of his stock was seized and taken away. The respondent defended the case, spending a sum of Rs. 10,895, and the prosecution ended in an acquittal on February 16, 1945. In his assessment to income-tax for the year 1945-46, the respondent claimed the deduction of the said sum of Rs. 10,895 from the profits of his business under section 10(2) (xv) of the Act. The Income-tax Officer

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disallowed the claim but the Appellate Assistant Commissioner allowed it, and his decision was confirmed by the Income-tax Appellate Tribunal, Calcutta Bench. Thereupon, the Commissioner of Income-tax, West Bengal, applied to the Tribunal to state a case for decision by the High Court under section 66-A of the Act, and the Tribunal accordingly referred the following question to that Court for its decision:—

Whether in the circumstances of this case the Tribunal was right in holding that the sum of Rs. 10,895 spent in defending the criminal proceeding was an expenditure laid out or expended wholly and exclusively for the purpose of business as contemplated by section 10(2) (xv) of the Indian Income-tax Act?

In dismissing the appeal preferred by the Income-tax Officer, the Tribunal observed:

"It may be stated straight off that it has not been established by any material that the conviction in cases like this may end in imprisonment. The question that personal liberty was likely to be jeopardised therefore will not be considered by us.....In any case, in the absence of any material in this particular case that personal liberty was likely to be jeopardised, all that we can say is that there was a chance of conviction in which the respondent might have been fined. No doubt, the element of saving himself from the fine, if any, might be there, but it is so inextricably mixed up with the main purpose for the defence that we are prepared to ignore that little element. In our opinion, the defence was solely for the purpose of maintaining his name as a good businessman and also to save his stock from being under-sold if the Court held that the prices charged by the respondent were unreasonable."

In the order made on the reference Harries C. J. (with whom Banerjee J. concurred) remarked:

"In every criminal prosecution where the matter is defended to protect the good name of a business or a professional man, the fear of possible fine or

imprisonment must always be there. But the Tribunal have pointed out that this was so inextricably mixed up with the protection of the good name of the business that it can well be found that the money spent in defence in the criminal prosecution was spent solely and exclusively for the purpose of the business. The finding is a finding of fact and is binding upon us."

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The learned Judges proceeded to refer to a ruling of the Bombay High Court—*J. B. Advani v. Commissioner of Income-tax*⁽¹⁾—and held that the respondent satisfied both the tests laid down there as applicable in such cases: He was charged with regard to a transaction which took place in the ordinary course of business and he was charged in his capacity as a trader. "If these two tests were satisfied and the Court came to the conclusion that the primary object of incurring the expenditure was to protect the good name of business, then it could be said that the expenditure was wholly and exclusively for the purposes of the business". The learned Judges accordingly answered the question referred to them in the affirmative. They, however, granted a certificate under section 66-A (2) of the Act that the case is a fit one for appeal to this Court.

We are unable to agree that the finding of the Tribunal, to which reference has been made, is binding on the Court as a finding of fact and is decisive of the reference. The finding of the Tribunal is vitiated by its refusal to consider the possibility of the criminal proceeding terminating in the conviction and imprisonment of the respondent. As has been stated, the respondent was prosecuted under section 13 which provides: "Whoever contravenes the provisions of this Ordinance shall be punishable with imprisonment for a term which may extend to five years or with fine or with both." The respondent was charged with contravention of section 6, which by sub-section (1) prohibits the sale by a dealer or producer of an article for a consideration which is unreasonable

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and sub-section (2) defines "unreasonable consideration". The framers of the Ordinance thus appear to have regarded the offence as one calling for a deterrent punishment in view of its anti-social character, and it is idle to suggest that it is for the Income-tax authorities to prove in such cases that the conviction might result in a sentence of imprisonment and that, in the absence of such proof, there was, at the most, only a chance of conviction and fine. We cannot appreciate the remark that "even this chance of conviction and fine was so inextricably mixed up with the main purpose of the defence that it could be ignored." A finding arrived at on this line of reasoning is obviously vitiated by a serious misapprehension regarding the risk involved in a prosecution under the Ordinance and it cannot be regarded as binding on the Court in dealing with the reference. If, as the High Court realised, in every criminal prosecution where the matter is defended to protect the good name of a business or a professional man, the fear of possible fine or imprisonment must always be there, it must ordinarily be difficult for any Court to say, that the expenses incurred for the defence, even if they are not to be regarded as the "personal expenses" of the person accused, constituted "expenditure laid out or expended wholly and exclusively for the purposes of the business". Learned counsel for the respondent frankly admitted that he was not able to find a single case in the books where the expenses incurred by a person exercising a trade or profession in defending a criminal prosecution, which arises out of his business or professional activities, were allowed to be deducted in the assessment of his profits or gains for income-tax purposes.

Reference was made in the course of argument to numerous cases where legal expenses incurred in civil litigation, arising out of matters incidental to the carrying on of a business, were allowed as a deduction in the computation of its profits, *e.g.*, *Commissioner of Income-tax v. Maharajadhiraj of Darbhanga*⁽¹⁾, where

(1) (1942) L.R. 69 I.A. 15.

the Privy Council held that law charges incurred in defending an action brought against a money-lender for damages for conspiracy, misrepresentation and breach of contract to advance sufficient funds to finance a company were allowable as business expenditure. In that class of case, no question could arise as to the primary or secondary purpose for which the legal expenses could be said to have been incurred as in the case of a criminal prosecution where the defence cannot easily be dissociated from the purpose of saving the accused person from a possible conviction and imposition of the prescribed penalty. Nor are we satisfied, as at present advised, that a distinction drawn in the Bombay case⁽¹⁾ between the legal expenses of a successful and unsuccessful defence is sound. The deductibility of such expenses 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. Income-tax assessments have to be made for every year and cannot be held up until the final result of a legal proceeding, which may pass through several courts, is announced.

For the reasons indicated we allow the appeal and answer the question referred in the negative. The appellant will be entitled to his costs both here and in the Court below.

Appeal allowed.

Agent for the appellant: *G. H. Rajadhyaksha.*

Agent for the respondent: *S. C. Banerjee.*

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(1) [1950] 18 I.T.R. 557.