In Re: The Assessment Of The Hindustan ... vs Unknown on 8 January, 1952

Equivalent citations: AIR1952ALL928

Author: V. Bhargava

Bench: V. Bhargava

JUDGMENT

Malik, C.J.

1. These are two references, one at the instance of the Commissioner of Income-tax and the other at the instance of the assessee.

2. The assessee is the Hindustan Commercial Bank, Ltd., with its head office at Kanpur. In the account year 1944-45 the assessee opened forty-six new branches, sub-branches and pay offices. In opening these new branches expenses were incurred and, while the assessee claims that the amount spent was a revenue expenditure deductible under Section 10 (2) (xv), Income-tax Act, on behalf of the Department it is claimed that the expenses incurred were in the nature of capital expenditure.

3. The Tribunal held that a part of the expenditure amounting to Rs. 89,870 was revenue expenditure and the balance, which came to Rs. 24,675-2-9, was capital expenditure. Though the Tribunal was of the opinion that the sum of Rs. 89,870 in round figures was revenue expenditure but as this was "deferred revenue expenditure" it spread it over a period of twenty years on the ground that the expenditure was of a heavy character, the benefits of which were likely to extend beyond the year in question upto that anticipated period. They, therefore, divided Rs. 89,870 by twenty and decided that the legitimate expenses per year were Rs. 4,493 for a period of twenty years.

4. The Commissioner of Income-tax filed an application (Reference Application No. 261 of 1947-43) that the following question be referred to this Court:

> "Whether in the circumstances and on the facts of the case, the sum of Rs. 89,870 in respect of expenses incurred in opening offices of the bank was an admissible deduction under Section 10 (2) (xii) now Section 10 (2) (xv) of the Act?"

5. The Tribunal was of the opinion that this was a question of law and has referred it to us under Section 66 (1), Income-tax Act.

6. On behalf of the assessee two applications were filed (Reference Applications Nos. 259 and 260 of 1947-48) with a prayer that the following three questions be referred to this Court for answer :

> "1. Whether in view of the finding that the expenditure of Rs. 89,870 is of a revenue nature and was incurred not to start any new business but to facilitate the carrying on of an existing business there was any legal justification for treating the amount as a deferred expen-diture and for spreading it over a period of 20 years and allowing only 1/20th of that amount during the year in question ?
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> 2. Whether in the circumstances of the case, charges for advertisement, entertainment, photos and invitation cards are of a revenue or capital nature?
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> 3. Whether in view of the fact that Rs. 10,000 have already been disallowed on account of inadmissible expenditure a further disallowance on the same question is legally justifiable without distinctly determining that the amount disallowed, namely Rs. 41,271-5-6 does not cover this amount of Rs. 10,000."

7. A difficulty has arisen, by reason of the very unsatisfactory way in which the statement of the case has been drafted, as to whether the Tribunal meant to refer the first two questions and disallowed the third, or they have referred to us only the first question and disallowed the second and the third. After hearing learned counsel on the point we are satisfied that the Tribunal meant to refer the first and the second question and disallowed the third. In para. 5 of the statement of the case the Tribunal said:

> "The following questions of law arise" and then quoted the question which arose in Reference No. 261 of 1947-48 on behalf of the Commissioner of Income-tax but did not number it.
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> The Tribunal then set out the first and the second question quoted above in the Reference Applications Nos. 259 and 260 of 1947-48 filed on behalf of the assessee and numbered them as "l" and "2". Paragraph 5 of the statement of the case, therefore, makes it clear that in the view of the Tribunal one question of law arose in the application filed on behalf of the Commissioner and two questions of law arose in the applications filed on behalf of the assessee. These two questions were, as we have already said, numbered as "l" and "2" as in the application for reference filed by the assessee.
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> In para. 6 of the statement of the case the Tribunal said:
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> "The third question sought to be referred is concluded by findings of fact and not referable."

Learned counsel for the Commissioner has urged that in para. 5 only three questions were mentioned and the third question referred to in para. 6 was the last question mentioned in para. 5.

We do not think that this is right. The Tribunal must have meant the third question framed by the assessee which related to a sum of Rs. 10,000 which the Tribunal had dealt with in para. 8 of its appellate order.

8. Coming now to the three questions mentioned above, we may take up the first question that arose in the assessee's application for reference, that is, whether the sum of Rs. 89,870 could be spread over a period of twenty years and allowance made at the rate of 1/20th each year. Learned counsel for the Commissioner has frankly admitted that he can find no provision in the Act for spreading out the expenditure over a period, of twenty years. If the amount was laid out and expended wholly and exclusively for the purpose of the business and was not in the nature of a capital expenditure, the whole of it was allowable under Section (10 (2) (xv) of the Act.

9. Our answer to this question, therefore, is in the negative viz. that there was no legal justification for spreading out the sum of Rs. 89,870 over a period of twenty years and the whole of the amount was deductable in that particular year, if it was not in the nature of a capital expenditure.

10. Taking up the question referred at the instance of the Commissioner and the second question referred to us at the instance of the assessee together, the details of these items of Rs. 89,870 and Rs. 24,675 and odd are given in the order of the appellate Assistant Commissioner as follows :

11. The sum of Rs. 24,675 consisted of the following items:

> Advertisement Rs. 5,444 Entertainment charges Rs.16,445 Invitation cards Rs. 2,085 Photographs Rs. 699

12. The other sum of Rs. 89,870 consisted of the following items:

> Salary Rs. 56,735 Dearnees allowance Rs. 5,229 Other allowances Rs. 4,355 Tax on salaries Rs. 3,059 Postage Rs. 690 G Telegrams Rs. 874 Telephone Rs. 1,112 Eent Rs. 10,882 Lighting Rs. 394 Travelling Expenses Rs. 6,385 Conveyance Rs. 147 From the statement of the case as well as from the order of the Appellate Tribunal it is clear that it was not disputed that these amounts were spent wholly and exclusively for the purpose of the business. The question, whether it was or was not so spent, was a question of fact and it was for the Tribunal to have decided the same. Prom the frame of the question and from the statement of the case it is clear that it was not in question whether the amount had been expended wholly and exclusively for the purpose of the business. The only point raised was whether this amount having been spent in connection with the opening of new branches, sub-branches and pay offices, it must be deemed to be an expenditure in the nature of a capital expenditure. From the nature of expenses indicated above, it is clear that the amount spent did not produce any new asset. It was incurred merely for the purpose of expanding the ordinary existing business of the company. Reliance has, however, been placed by Sri Das on the observations of Lord Cave in Atherton v. British Insulated and Helsby Cables Ltd., (1926) 10 Tax Cas. 155 at p. 159 which are as follows:

> "An expenditure to be in the nature of a capital expenditure should not only have been incurred once and for all, but with a view to bringing into existence an asset or an advantage for the enduring benefit of a trade."

Learned counsel has urged that this expenditure was incurred only once and for all and by reason of the opening of the new branches the company has got an advantage for the enduring benefit of the trade or business carried on by it.

In the case before the House of Lords the company, British Insulated and Helsby Cables, Ltd., had contributed a sum of lb. 31,784 to a pension fund to enable the elder members of the existing staff being admitted to the benefits of that fund without any additional contributions on account of their age. It was urged on behalf of the assessee that the amount did not remain in the company's hands but was irrevocably paid away to the trustees of the Pension Funds. Their Lordships held that that expenditure was in the nature of a capital expenditure and brought into existence an advantage for the enduring benefit of the trade and explained it in the latter part of the speech of Lord Cave where his Lordship said:

> "The object and effect of the payment of this large sum was to enable the Company to establish the Pension Fund and to offer to all its existing and future employees a sure provision for their old age, and so to obtain for the Company the substantial and lasting advantage of being in a position throughout its business life to secure and retain the services of a contented and efficient staff."

His Lordship quoted with approval the decision in Ounsworth v. Vickers, (1915) 3 K. B. 267 that an expenditure incurred by a ship-building firm in deepening a channel and creating a deep water berth (not on their own property) to enable vessels constructed by them to put out to sea was in the nature of capital expenditure and was not deductable under the Income-tax Acts. It is urged that the opening of new branches was an advantage for the enduring benefit of the business and was in the nature of capital expenditure.

13. Every expenditure incurred by a business concern for the purpose of its business is bound to result in some benefit to its business and, the mere fact, that the benefit is not confined to one year, does not to our minds answer the question. Every business man who carries on business wants to carry on his business not only at the scale at which he had been doing it but also wants to extend it as much as he can. It is one of the ordinary incidents of a business. Section 10 (2) (xv) does not define what is in the nature of a capital expenditure and what is a revenue expenditure, but in several cases an attempt has been made to explain the same. Learned counsel have cited several decisions and we shall discuss them later but it is admitted that there has been no direct case on the point whether an expenditure incurred in connection with starting of a new branch--the nature of the business remaining the same--is ail expenditure in the nature of a capital expenditure or a revenue expenditure.

It must be conceded on behalf of the Department that if the assessee increased its business at the place where it was being carried on by advertisement in the papers or other such means e. g.,

employment of new staff, or by giving special facility to its constituents, that would be normally revenue expenditure. The mere fact that for the purpose of carrying on the same type of business and to attract more business they opened other branches at different places and incurred expenses which did not produce any new asset, that does not to our minds seem to change the nature of the expenditure. It is not a case where an assessee had started a new line of business or acquired new premises or purchased other assets which could be included as an asset in the profits and loss account.

It is merely a case where for the purpose of extending the business new branches had been opened and certain expenses had been incurred by way of advertisement etc. We think that it cannot be said that an expenditure of this kind brings in an advantage for the enduring benefit of trade and is, therefore, capital expenditure.

14. The cases cited by learned counsel for the parties are as follows though none of them appears to be very helpful.

15. (1) Commr. of Income-tax, Madras v. Siddareddy Venkatasubba Reddy and Bros., Guntur, 1949-17 I. T. R. 15 (Mad.) There the assessees who were carrying on the business of winning mica and selling it after refinement entered into certain agreements under which in consideration of payment of sums of money in instalments they were granted the mining rights in different plots of land. Reliance is placed on the observations of the learned Chief Justice which are as follows:

> "In a broad sense, an assesses can be said to carry on a particular kind of business, but it may consist in several separate ventures. While carrying on an already existing business, there may be an extension of a business, there may be a substantial replacement of equipment. In all such cases, the expenditure incurred for starting new ventures, for extending the business and for replacing equipment cannot be treated as revenue expenditure."

These observations must be confined to the facts of that case and it is clear that in that case new assets had come into existence as new mining rights in different plots of land had been acquired.

16. (2) The Commr. of Inland Revenue v. The Granite City Steamship Co. Ltd., (1929) 13 Tax Cas 1. In that case the assessee owned one ship only which was seized in 1914 by the German Government and handed back to the assessee in 1918 in a condition which necessitated extensive repairs. These repairs were completed at a cost of . 10,152. The assessee claimed to deduct this amount in computing for Income-tax purposes their profits for that year. It was held that the necessity for the repairs had not arisen out of the use of the ship by the assessee in earning their profits and the cost of repairs was a capital expenditure. Eeliance is placed on the following observations of Lord Sands at page 14 :

> "Broadly speaking, outlay is deemed to be capital when it is made for the initiation of a business for extension of a business, or for a substantial replacement of equipment." and again at page 15.

> "As I indicated at the outset, expenditure may be capital expenditure by reason of its being initial expenditure and not expenditure incurred in carrying on a business."

It cannot be said that this was in the nature of a new expenditure inasmuch as the business was being carried on from before and the observations of Lord Sands quoted above cannot be interpreted to mean that every kind of expenditure incurred for extension of a business must be capital expenditure. In fact the use of the words 'broadly speaking, outlay is deemed to be capital' at the beginning make it clear that it would depend upon the nature of the expenditure incurred. We have already given the details of the expenditure in this case and in our view such expenditure cannot be said to be capital expenditure merely because it helped in extending the business of the assessee.

17. Eeliance is also placed on the judgment of Lord Hanworth in Eastmans Ltd. v. Shaw (H. M. Inspector of Taxes) (1929) 14 Tax Cas. 218 at p. 226 which is as follows:

> "Upon the facts found it appearsto me that the principle of law is clear, and has been rightly applied by the Commissioners and by Rowlatt, J. that these expenses were incurred anterior to the business or trade which was carried on by this Company, that it was in the nature of a capital outlay and a capital loss, and was not to be treated as money wholly and exclusively laid out for the purpose of profit."

In that case the assessee Company carried on business as butchers and meat retailers and had a very large number of shops varying between 1,447 in 1911 and 804 in 1922. The policy of the Company was to close shops or to open shops in accordance with the needs of their business as a whole and they found it advantageous to dispose of the fixtures and fittings in a shop given up rather than to transfer them to a newly acquired shop. In such circumstances the Company debited in their trading account the difference between the cost of new fixtures and the price obtained for old fixtures and it was held that no deduction was admissible in computing the Company's profits in respect of the excess of the cost of new fixtures over the price obtained for the old fixtures. These expenses were incurred when a new branch was opened.

Sri Pathak has, however, urged that time is not the material factor in the determination of the question whether the expenses incurred were in the nature of a capital expenditure or a revenue expenditure. He has relied on Mohanlal Hargovind of Jubbulpore v. Commr. of Income-tax, C. P. and Berar, Nagpur, 1949-17 I. T. r. 473 (P. C.) where, for the facility of business, an agreement was entered into to acquire the exclusive right to collect tendu leaves and their Lordships held that it was in the nature of a revenue expenditure. The facts of these cases are clearly distinguishable and we need not, therefore, consider them any further.

18. Eeliance is placed on a decision of this Court in the Jagat Bus Service, Saharanpur v. Commr. of Income-tax, U. P. and Ajmer-Mer-wara, 1950-18 I. T. R. 13 (ALL) by a bench of which one of us was a member. The observations at 22 are to our minds of considerable assistance and support the conclusion to which we have arrived. It was said as follows:

"The decision in each case, of the question, whether an item of expenditure is revenue expenditure or capital expenditure, depends upon a variety of circumstances, e.g. the nature of the expenditure, the source from which the money was spent, whether the payment was made once and for all or is a recurring expenditure and whether the asset acquired is going to be a source of permanent income or it exhausts itself either during the course of the year when it was acquired or within a short period thereafter. The main test is its permanency, i.e., whether the value of the capital of the company or its asset or its goodwill is permanently increased by reason of such expenditure.

It is impossible to lay down any test which would meet all eases. For example, a firm carrying on the business of plying motor vehicles for hire might decide to increase its business and lay down a new road connecting two places. This would be in the nature of a capital expenditure. If, on the other hand, it spends money every year for the running repairs to the road, that might be in the nature of a revenue expenditure. Similarly, a firm dealing in machinery might buy machinery for sale which would be revenue expenditure, while an industrial concern might buy machinery to replace worn out machinery and that would be in the nature of capital expenditure. Even in the case of an industrial concern minor repairs which have to be frequently made and which are known as running repairs are revenue expenditure, while replacement of costly machinery is capital expenditure.

It is, therefore, difficult to lay down any test which could be applied to every case. To my mind, 'capital' means an asset which has an element of permanency about it and which is capable of being a source of income and 'capital expenditure' must, therefore, generally mean an acquisition of an asset and the asset must be intended to be of lasting value; while income or revenue expenses are generally running expenses incurred in earning profit or expenses incurred with the primary object of an immediate return or acquisition of assets which are not of lasting value and are likely to get exhausted or consumed in the process of the return or a very limited number of returns."

In Atherton v. British Insulated and Helsby Gables, Ltd., (1926-10 Tax. Cas. 155) their Lordships held that a new asset of lasting value was acquired inasmuch as there was lasting advantage for securing the services of a contented and efficient staff. In the case before us all that has happened is that by reason of opening of new branches the out-turn of the business may have increased on which the assesses is liable to pay tax. It cannot be said in this case that there has been any such acquisition of an asset which would amount to all the expenses being classed as capital expenditure.

19. The result, therefore, is that in our view the amount of Rs. 89,870/- was in the nature of a revenue expenditure and was not in the nature of a capital expenditure.

20. In regard to the sum of Rs. 24,675/- there is a further argument advanced that expenses incurred in a special campaign of advertisement cannot be deemed to be revenue expenditure. This

would mean that the Income-tax Department would have to judge in each case the amount of advertisement expenses that a particular business is entitled to spend to facilitate its business and any sum spent in excess of that would have to be disallowed as not permissible expenditure.

21. Advertisement has now become a very common feature of every business and the amount is always spent to facilitate the business and to get better returns. No case has been cited before us in which it has been held that the amount spent in 'a special campaign of advertisement' must necessarily be a capital expenditure. Reliance is placed on a passage in Sundaram's Law of Income-

tax in India, 1947 Edn. page 636 which is as follows:

> "Thus, advertisement charges would be allowed if they were incurred for selling the goods in the ordinary course, but if a special campaign of advertisement was launched, say, for expanding the business or floating a new company or extending the activities of the business in new directions the expenditure would be disallowed."
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> Sri Pathak objects to this being relied upon on the ground that these are observations of a living author. But for the fact that this passage was quoted in the order of the Appellate Tribunal, though reference was not made to Sundaram's book we would not have made any reference to it. All that we need say is that we find no authority for the view that a special campaign of advertisement merely for the purpose of extending the business, must be deemed to be a capital expenditure and not allowable as a permissible deduction under Section 10 (2) (xv), Income-tax Act. The Tribunal has quoted a decision in Watney v. Musgrave, (1881-
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> 88) 1 Tax. Cas. 272. We have carefully considered that case and are of the opinion that that case does not support the proposition laid down. In that case a brewer had taken a lease of a public house for purposes of letting it out to tenants under covenants to buy beer brewed by him alone and had paid premium for the lease which was for a period of thirty years and the question was whether he was entitled to take all the amount paid by him as premium.

The point turned on the decision of the question whether the amount paid as premium could be treated as a part of expenses of production of the beer. The learned Judges were of the opinion that it could not be so done. We need quote a passage from that judgment which is as follows :

> "Now, for the first time, as far as I am aware, it is sought to include in the sum to be deducted, so as to ascertain the balance which would constitute the net profits of the concern, gums of money expended, not in the manufacture, but after the production of the article in order to promote the sale or increase the quantities sold .... I am not, however, aware that any attempt has been made hitherto to claim to deduct the costs of advertisements, by means of which the quantity of beer sold in the course of the year may be considerably in creased, but which has no reference to, and bears no part at all in, the production of the article.

> The present case is an instance, not of advertisements, but of expenses incurred to induce a publican or class of publicans to purchase quantities of beer. It may be necessary to take those expenses into consideration in ascertaining the net profits of a commercial firm during any given year or time, but inasmuch as it has never been argued or even suggested that such expenses should be taken into consideration, in ascertaining the difference between the cost of production and the money realised during the course of the year by the sale of the beer, for the purposes of the income-tax, I do not think we ought to deal with this in the way suggested."

The expenses incurred in entertainment, photographs and invitation cards are more or less for the same purpose i.e. advertisement. We may make it clear that we have assumed as it was not open to us to go into the question, that these expenses were incurred wholly and exclusively for the purpose of the business.

22. We are, therefore, of the opinion that the sums of Rs. 89,870/- and Rs. 24,675/- were in the nature of revenue expenditure and were admissible to deduction under Section 10 (2) (xv) of the Act.

23. The assessee is entitled to its costs which we assess at Rs. 500/-.