proved by summoning the records of the Postal Department or by producing the registered cover with dates of franking of the postage stamps and cover etc. The absence of all this evidence leads us to doubt whether any such papers had at all been sent to the appellant by his mother. It has been argued by Shri Aggarwal on the basis of *Sohan Lal's case* (1) (supra) that some vague information about the passing of some sort of decree would not be enough. In the present case, the appellant had all the necessary particulars about the case and the Court from the notices and other papers affixed at his place of residence. These particulars could also have been supplied to the appellant by his co-respondent who was living in the same house. The husband of the lady had been examined in Court and had stated that he had secured the documents pertaining to the case from the District Courts at Delhi and that thereafter he had a talk about it with the appellant. A husband would naturally have something to say to a person who had brought such infamy to his wife and for having repaid them in this manner for the shelter giving in the house. The appellant, therefore, fails to satisfy me that he had any sufficient cause for his non-appearance on so many dates of hearing or that he had applied within time.

(11) The appeal fails and is hereby dismissed with costs which shall include the conditional costs remaining unpaid in compliance with the Court's order dated 8th March, 1971.

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*N. K. S.*

INCOME-TAX REFERENCT

*Before D. K. Mahajan and H. R. Sodhi, JJ.*

THE COMMISSIONER OF INCOME-TAX, PUNJAB, J.&K. AND CHANDIGARH, PATIALA,—*Applicant.*

*versus*

THE ORIENTAL CARPET MANUFACTURERS (INDIA) PRIVATE LTD., AMRITSAR,—*Respondent.*

**Income tax Reference No. 2 of 1971.**
July 27, 1971.

*Income-tax Act (XI of 1922)—Section 10(2)(xv)—Company not doing business of its own but deriving income from dividends received from its*

The Commissioner of Income-tax, Punjab, J.&K. and Chandigarh, Patiala *v.* The Oriental Carpet Manufacturers (India) Private Ltd., Amritsar.
(Mahajan, J.)

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*subsidiary companies—Such parent company rendering certain services to subsidiary companies—Expenditure so incurred for services, charged to the subsidiary companies—Such expenditure—Whether allowable deduction as business expenditure from the income of the subsidiary companies under section* 10(2)(*xv*).

*Held,* that a company not carrying on its own business, derives income from its subsidiary companies. Such parent company, however, renders certain services to the subsidiary companies and the expenses so incurred are recovered by it in proportion to the paid-up capital of the subsidiary companies. This expenditure is an allowable deduction under section 10(2)(xv) of Income-tax Act, 1922 as business expenditure of subsidiary companies. The subsidiary companies do their own business and what the parent company does for them can also be done by them and they can claim deduction, but this will involve more expenditure to them. For that reason the arrangement is arrived at between the subsidiary companies and the parent company. There is no distinction in principle between the business expenditure incurred by the subsidiary companies and the business expenditure incurred by the parent company for them.

*Reference made under Section* 66(2) *of the Indian Income-tax Act,* 1922 *made by the Income-tax Appellate Tribunal (Chandigarh Bench) for opinion to this Hon'ble Court on the following question of law in R.A. No.* 409 *of* 1964-65 *arising out of I.T.A No.* 9729 *of* 62-63 *regarding Assessment year* 1957-58:—

> "*Whether on the facts and in the circumstances of the case the amount of Rs.* 36,966 *charged to the assessee company by M/s. Oriental Carpet Manufacturers (London) Ltd. was not an allowable deduction under section* 10(2)(*xv*) *of the Income-tax Act,* 1922."

D. N. Awasthy and B. S. Gupta, Advocates, for the appellant.

Kirpa Ram Bajaj, Senior Advocate with Prem Nath Moonga, and B. S. Chawla, Advocates, for the respondent.

## JUDGMENT

Mahajan, J.—(1) This reference raises a very interesting question. There is no direct authority on the point. However, the cases cited at the bar do throw some light in determining the controversy.

(2) This reference has been made by the Income-tax Appellate Tribunal, Chandigarh Bench. The question referred for our opinion is as follows :—

> "Whether on the facts and in the circumstances of the case the amount of Rs. 36,966 charged to the assessee company by M/s Oriental Carpet Manufacturers (London) Ltd. was not an allowable deduction under-section 10(2) (xv) of the Income-tax Act, 1922."

This question has arisen out of the decision rendered by the Income-tax Appellate Tribunal, Delhi Bench 'B'.

(3) On the facts leading to the reference, there is no dispute. The parent company is Messrs Oriental Carpet Manufacturers (London) Ltd. It has six subsidiary companies, namely :—

(1) East India Carpet Manufacturing Co., Ltd., Amritsar.

(2) E. Hills & Co., Pvt. Ltd., Mirzapur.

(3) Oriental Carpet Manufacturers (Canada) Ltd., Toronto.

(4) Oriental Carpet Manufacturers Co. (London) Pvt. Ltd.

(5) Fritz & La Rue Company, New York.

(6) The Oriental Carpet Manufacturers (India) Private Ltd., Amritsar—the assessee company.

The parent company (Messrs. Oriental Carpet Manufacturers (London) Ltd.) (hereinafter referred to as the parent company) does not carry on its own business. Its only source of income is dividends received from its six subsidiary companies. The parent company, however, renders certain services to the subsidiary companies, namly :—

(a) Arranged for overdraft facilities.

(b) Stood surety for Rs. 14 lakhs for the assessee company for loans advanced by National & Grindlays Bank Ltd.

(c) Advanced large amounts to the assessee company for business purposes without charging interest.

(d) Rendered advice on technical and business matters, export market expenditure for the work done for the subsidiary companies.

The expenses so incurred are recovered by the parent company in proportion to the paid-up capital of the subsidiary companies.

(4) The dispute in the present reference relates to the assessment year 1957-58, the previous year ending on 31st December, 1956. The total expenditure incurred by the parent company during this assessment year amounted to £20,071. The parent company deducted an amount of £3,903 on account of the expenses incurred by it. The balance £16,168 was distributed by the parent company towards the expenses incurred by it on behalf of the subsidiary companies in proportion to the paid-up capital of those companies. The amount that fell to the share of the assessee-company is £2,072, or converted into rupees, Rs. 36,966. This amount was claimed by the assessee company as deduction on account of "Central Office Administrative Expenses". The claim was made under section 10(2) (xv) of the Indian Income-tax, 1922.

(5) The income-tax Officer disallowed the assessee's claim by his order dated 26th March, 1962. The relevant part of the order reads thus :—

> "Thus it is clear that the holding company (parent company) is incurring these expenses for its own purpose of ensuring that the capital sunk by that company entirely in the subsidiaries is properly supervised and controlled and is ultimately duly rewarding in the form of dividends."

An appeal was taken by the assessee to the Appellate Assistant Commissioner of Income-tax, Amritsar Range, and the Appellate Assistant Commissioner affirmed the decision of the Income-tax Officer for the same reasons which prevailed with the Income-tax Officer. The assessee preferred a second appeal to the Income-tax Appellate Tribunal Delhi Bench 'B' and the Tribunal allowed the claim with the following observations :—

> "The assessee company has made its claim for deduction under section 10(2) (xv). Two conditions must be satisfied before it can be allowed. The first condition is that the disputed amount should have been spent by it wholly and exclusively for the purpose of its business. The second condition is that the expense should not be of a capital nature. The assessee has satisfactorily established the fact that the parent company arranges in U.K. for the

overdraft facilities to be granted to it in India. The parent company stands as a surety to the extent of Rs. 14 lacs. The parent company advances loans to the assessee company for its business without charging any interest. In addition to this the parent company advises the assessee company on all technical matters, business conditions and prospects etc. It is clear that the parent company is under no legal obligation to render all this assistance to the assessee company. It is equally clear that but for the parent company's undertaking to do all this, the assessee company would have been obliged to open its own office in London or to have some agent there to perform all these functions. It cannot be disputed that the parent company has to spend large amounts for discharging all these functions. Besides it has to run the risk of being a surety. Out of the total expense of £20,071, £10,294 have been spent under the head 'Salaries' and General charges; £698 under the head 'Pensions and Benefits'; £400 towards the audit fee; £3,900 towards Director's remuneration; £4,449 for other emoluments and £330 towards pension. By common arrangement all the subsidiary companies have entrusted the parent company with their function in London and have evolved a formula for apportioning the expenses incurred by the parent company. It is clear from all this that the disputed amount is the assessee company's contribution to the parent company towards the expenses incurred by the parent company for attending to its business affairs and rendering other assistance etc. abroad. The disputed amount is obviously incurred for its business purpose and is of course of a revenue nature. The formula by which the total expense is distributed amongst the several companies is a fair and reasonable formula."

(6) The Department being dissatisfied moved the Income-tax Appellate Tribunal under section 66(1) of the Income-tax Act, 1922, and the Tribunal refused to refer the question of law on the ground that no question of law arose. The Department then moved this Court under section 66(2) and this Court directed that the question already stated be referred for the opinion of this Court. That is how, the Income-tax Appellate Tribunal, Chandigarh Bench has referred the said question of law for our opinion.

(7) Mr. Awasthy, in the first instance, contended that the amount expended by the subsidiary company towards the expenses of the parent company was of a capital nature. However, this was not the case of the Department either before the Income-tax Officer or before the Appellate Assistant Commissioner or the Tribunal. This argument does not at all arise either out of the question referred or out of the order of the Tribunal and therefore, we have declined him to pursue this matter any further.

(8) Mr. Awasthy then contended that the expenditure incurred by the parent company which is being reimbursed by the assessee-company has been incurred wholly and exclusively by the parent company for its own business. The learned counsel does not dispute that if this expenditure has been incurred by the assessee company for its business, his contention that deduction should not have been allowed under section 10(2) (xv) would not stand. His contention is that this expenditure has been incurred by the parent company to earn higher profit, the implication being that earning profit on its investment is the business of the parent company. Mr. Awasthy relies on certain observations in *Odhams Press Ltd.* v. *Cook*, (1). There can be no two opinions that the assessee is only entitled to deduction under section 10(2) (xv) if it could satisfy the Tribunal that the expenditure was wholly and exclusively incurred for its own business. The Tribunal has found as a fact that it was so incurred. Therefore, on the findings of the Tribunal the argument is not open to the learned counsel for the Department that the expenditure should be treated as having been incurred by the parent company for its own business. The Tribunal nowhere found that it was so.

(9) It will be useful at this stage to refer to the observations of Lord Chancellor in *Odhams Press Ltd. case* (1) :—

> "Now these facts seem to me to be evidence upon which the Special Commissioner might reasonably arrive at the conclusion that the sum written off was not so written off wholly and exclusively for the trade and business of the Appellants. No doubt it was better for the Appellants that their subsidiary companies, and this one amongst them, should prosper, and not be weighed down with debts. The

(1) (1941) 19 I.T.R. (Supplement) 92.

same would be equally true of any company holding shares in another company and having trading relations with it. It is tempting to treat what I have called the subsidiary company as if it was part and parcel of the Appellants, but, as the Master of the Rolls points out, the two companies are separate taxable persons. The trade or business of one company, even though it may affect very closely the trade or business of another, is not the same as that other's trade or business. Rule 3(a) of the Rules applicable to Cases I and II of Schedule D prohibits the deduction of 'any disbursements or expenses, not being money wholly and exclusively laid out or expended for the purposes of the trade', that is to say, the trade of the person whose profits or gains are being computed. The Appellants were computing their profits and gains, and it is their trade which is to be regarded. The Special Commissioner finds, on evidence of which there is abundance, that the 'sum written off was not so written off wholly and exclusively for the purpose of the trade or business of the Appellants'. That is enough to shut out the Appellants' right to deduct the amount.

It was suggested, through I think not very strenuously, by the Appellants' counsel that Rule 3(a) was not germane to the facts of this case, because the writing off of the sum in question was not a disbursement or expense, but was in the nature of a tradesman's discount or rebate. That is not the view taken by the Special Commissioners of the facts, nor do I think it is the right view. The sum of £2,927 5s. 8d. was the exact amount of the trading loss of the subsidiary company for the year in question, and bore no relation whatever to the prices charged by the Appellants for the work they had done."

(10) These observations do not seem to support the contention of the learned counsel. If at all, they lend support to the case of the assessee. Mr. Awasthy then tried to draw some support from the observations of Viscount Maugham at page 109 of the report :—

"My Lords, there can be no doubt that limited companies who carry on business are separate taxable persons, and the profits and gains of their several businesses are separate

profits and gains for the purposes of the Income-tax Acts. This is none the less true if one of the companies should be the parent company, and the other or others may be its subsidiaries of which the shares are held or owned by the parent company.

It is equally plain that the Appellants stood towards Coming Fashions, Ltd., in a two-fold relationship. They were, in a sense, proprietors of that concern, in so far as they held all the shares in it. Its dividends, if any, came to the Appellants, and on a winding up of Coming Fashions, Ltd., its assets after payments of debts, liabilities and costs would be the property of the Appellants. On the other hand, there was also another and a quite different relationship between the two companies, that of tradesman and customer. It should be added that there is no suggestion that the sum of £2,927 was written off as a bad debt."

Even these observations do not help the learned counsel.

(11) It will be proper at this stage to set out the facts of *Odhams Press' case* (1) to appreciate the Tribunal's decision :—

"The Appellants are printers and publishers, and they hold controlling interests in some sixteen subsidiary companies, which own newspapers or other publications, or are printers, publishers, advertising agents, or carry on similar businesses. In particular, the Appellants hold all the sharers in Coming Fashions Ltd., which compiles and issues for sale a periodical called 'Every-woman's'. The Appellants publish this periodical for Coming Fashions, Ltd., upon a commercial basis, and from time to time have advanced on loan large sums to that company. In addition to the amounts advanced, the Appellants were owed by the company at the 31st December, 1933, a sum of £10,118 on trading accounts representing charges for work done at full trade prices. For the trading year ending the 31st December, 1933, Coming Fashions Ltd., made a net trading loss of £2,927.5s. 8d. The Appellants wrote off in their own accounts an amount equal to this loss from the amounts due

to them by Coming Fashions Ltd., on trading account. It is this sum so written off that the Appellants allege that they are entitled to deduct in commuting the profits and gains of their trade for the year ending the 31st December, 1933. They rely on Case I, Schedule D, of the Income-tax Act, 1918. It may be mentioned that a similar question arises under another year of assessment."

(12) If these facts are kept in view, the entire *ratio* of the decision would be apparent. As already pointed out, the crux of the matter is whether the expenditure in question is the business expenditure of the subsidiary company or is it the business expenditure of the parent company. It is plain that the parent company does no business. All it does is to earn dividend from its investments, if that can at all be called a business. The subsidiary companies do business and what the parent company does for them could have been done by these subsidiary companies themselves. This would have involved more expenditure to the subsidiary companies and for that reason the present arrangement has been arrived at between the subsidiary companies and the parent company. We put it to Mr. Awasthy what would be the difference in the present case and in a case where a number of principals join together to appoint a common agent in order to further their own business transactions and that agent incurs expenditure on behalf of each of the principals and charges that expenditure from the principals. The learned counsel was unable to give us any satisfactory answer. It is not contended that in such a case the expenditure incurred by the principals would be expenditure chargeable to tax under section 10(2). In principle, we see no distinction between the present case and the case which we have put to the counsel by way of illustration.

(13) In our opinion, the Tribunal was right in the circumstances and on the facts of the present case in coming to the conclusion that the assessee-company was entitled to claim this deduction under section 10(2)(xv). We see no escape from this conclusion.

(14) For the reasons recorded above, we answer the question referred to us in the negative, that is, in favour of the assessee and against the Department. In view of the difficult nature of the question involved, we make no order as to costs.

*N. K. S.*