Commissioner of Income Tax Vs Jiyajeerao Cotton Mills Ltd.

Court: Calcutta High Court

Date of Decision: Jan. 25, 1990

Acts Referred: Income Tax Act, 1922 â€" Section 10(2)(xv)
Income Tax Act, 1961 â€" Section 256(2), 28, 29, 30, 30

Citation: (1995) 79 TAXMAN 51

Hon'ble Judges: Suhas Chandra Sen, J; Bhagabatiprasad Banerjee, J

Bench: Division Bench

Advocate: A.C. Moitra and R.C. Prosad, for the Appellant;D. Pal, J.P. Khaitan, R.N. Bajoria and A.K. Dey, for the Respondent

Judgement

Suhas Chandra Sen, J.
The Tribunal has referred the following questions of law to this Court u/s 256(2) of the income tax Act, 1961 ("the

Act"):

1. Whether, on the facts and in the circumstances of the case, the Tribunal misdirected itself in law in holding that the assessee is entitled to relief

u/s 80I in respect of proportionate managing agency commission amounting to Rs. 1,85,061 for the assessment year 1968-69 ?

2. Whether, on the facts and in the circumstances of the case, the Tribunal was right in law in holding that relief/deduction u/s 80I should be

allowed with reference to the profit and gains from priority industry without deducting proportionate managing agency commission therefrom?

3. Whether, on the facts and in the circumstances of the case, the Tribunal was right in law in holding that for the purpose of allowing deduction or

relief u/s 80I of the income tax Act, 1961 commercial or accounting profits should be taken to be the actual profits ?

4. Whether, on the facts and in the circumstances of the case, the Tribunal having held that the accounting profits as worked out by the assessee

should be the commercial profits for the purpose of section 80I of the income tax Act, 1961, the conclusion of the Tribunal that the assessee is

entitled to additional deduction u/s 80I of the said Act in respect of the proportionate managing agency commission that had been allowed as

deduction in computing the business income if the assessee is unreasonable and/or perverse ?

The assessment years involved are 1968-69 and 1969-70. The accounting periods are year ended on 31-3-1968 and 31-3-1969, respectively.

2. In the statement of the case the Tribunal has also mentioned three other questions in paragraph 4 as to have been directed to be referred in

Matter No. 189 of 1978. But it appears in the order passed by this Court that the Rule was issued only in respect of the question which has been

referred hereinabove and the Rule was made absolute with regard to that question in a proceeding u/s 256(2).

3. It appears from the records of section 256(2) proceedings, being Matter No. 189 of 1978, that a Rule was issued in respect of all the four

questions by the revenue by order dated 18-9-1978. Ultimately when the case was taken up for final hearing the Rule was made absolute only on

question No. 1 which has been set out hereinabove. Rule in respect of all other questions was discharged.

4. The facts out of which the controversy arose have been stated by the Tribunal as under:

The assessee claimed relief u/s 80I of the income tax Act, 1961 in respect of its unit, Sourastra Chemicals. There is no dispute that the aforesaid

unit had been engaged in a priority industry and the assessee was entitled to relief u/s 80I in respect thereof. The assessee submitted to the ITO its

computation of relief u/s 80I and the amount of relief claimed was Rs. 2,10,489 and Rs. 7,90,028 for the assessment years 1968-69 and 1969-

70, respectively. For the assessment year 1968-69 the assessee-company started its computation with reference to the loss of Rs. 19,17,512 as

per profit and loss account and no profit was computed at Rs. 26,31,123 and 8 per cent thereof was worked out to Rs. 2,10,489. The profit as

per profit and loss account for the assessment year 1969-70 was Rs. 75,75,429, net profit was computed at Rs. 98,75,356 and 8 per cent thereof

was worked out to Rs. 7,50,023. The assessee arrivedat net profit for the assessment years 1968-69 and 1969-70 for the purpose of section 80I

after deducting proportionate managing agency commission of Rs. 1,85,061 and Rs. 5,89,130 respectively. Development rebates of Rs.

20,79,000 and Rs. 3,57,600 for the respective two assessment years were added to the profits disclosed as per profit and loss account or

deducted from the loss as per profit and loss account. Similarly, in working out the profit for purpose of section 80I the assessee added the interest

paid as head office or deducted from the loss as per profit and loss account of such interest paid to head office. Interest paid to head office was

Rs. 25,12,850 and Rs. 21,83,355 for the assessment years 1968-69 and 1969-70 respectively.

The ITO, on the other hand, computed the profit for the two assessment years at Rs. 9,79,120 and Rs. 86,580, respectively. Relief was worked

out by applying 8 per cent of the aforesaid amount of net profit for each of the assessment years. He took net profit as per profit and loss account

for the respective assessment years at Rs. 5,95,338 and Rs. 97,63,784. The ITO followed the assessee in regard to the deduction of

proportionate managing remuneration for the purpose of section 80I but unlike the assessee he deducted the development rebate for finding out the

net profit in order to compute the relief u/s 80I. There was slight difference in ITO"s computation of development rebate allowable to the assessee.

These figures for the respective assessment years were Rs. 20,79,082 and Rs. 8,57,613. In this regard it may be mentioned that the assessee

credited development rebate reserve by debiting the profit and loss account with amount equivalent to development rebate.

Being aggrieved, the assessee appealed before the AAC and contended before him that the deduction u/s 80I should have been allowed with

reference to the profit and gains from the priority industry without deducting development rebate and proportionate managing agency commission

from the same. It was submitted that the deduction had to be worked out on the profit and gains of the priority industry and not on the assessable

income. In regard to the development rebate it was the assessee"s case that extra benefit or incentive to the assessee should not be treated as an

expenditure necessary for working out the profits and similarly proportionate managing agency remuneration should not also have been deducted.

The AAC expressed inability to accede to the assessee"s submission. According to him, the profit and gains of a priority industry for the purpose

of section 80I should be computed after taking into account the deductions specified in sections 28 to 44 and as the ITO had actually done so, he

refused to interfere with the matter. The assessee felt aggrieved by the AAC"s decision and preferred appeals before the Appellate Tribunal.

Before the Tribunal the assessee objected to the decision taken by the AAC on the ground that development rebate was not normal business

expenditure but a benefit extended to the assessee only on fulfilling prerequisite conditions. According to the assessee, section 80I envisages relief

as an encouragement to the companies engaged in priority industries under certain specified conditions. It was contended that the profit and gains

attributable to a priority industry need not be computed after allowing all the deductions admissible in computing the business income under

sections 30 to 43 of the income tax Act, 1961. The assessee also contended before the Tribunal that though it had deducted proportionate

managing agency remuneration in its computation for the assessment years 1968-69 and 1969-70, the ITO should have applied the proper law

following the decisions of the Supreme Court in Commissioner of Income Tax, Bombay Vs. C Parakh and Co. (India) Ltd., and Commissioner of

Income Tax, Bombay Vs. Maharashtra Sugar Mills Ltd., Bombay, .

The Tribunal held :

After going through the authorities cited before us and considering all the rival submissions on the basis of the facts and circumstances of the case,

we are of the opinion that the assessee should be entitled to further relief u/s 80I in respect of proportionate managing agency commission of Rs.

1,85,061 and Rs. 5,89,130 for the assessment years 1968-69 and 1969-70 respectively. For attaining this relief, we are in complete agreement

with the contention taken up by the learned counsel for the assessee who relied on the decisions of the Supreme Court in Commissioner of Income

Tax, Bombay Vs. C Parakh and Co. (India) Ltd., and Commissioner of Income Tax, Bombay Vs. Maharashtra Sugar Mills Ltd., Bombay, . It is

now well-settled that the income tax authorities must not deduct proportionate managing agency commission while computing income of a branch.

In other words, managing agency commission payable by a company to its managing agents related to the finally determined profits of the

company. In the instant case before us the assessee-company paid managing agency commission to Birla Gwalior Ltd. The assessee might have

debited such proportionate managing agency commission in the accounts of its different units. But this would not in our opinion prevent the

assessee from availing of the benefit which is otherwise due to it under the law. Therefore, we direct the ITO to revise his orders for the aforesaid

two assessment years, i.e., 1968-69 and 1969-70 by allowing additional deduction u/s 80I in respect of the proportionate managing agency

commission to the assessee.

5. Section 80 is one of the sections in Chapter VIA of the Act. The scheme of the Act is that the total income of an assessee is first to be

computed in accordance with the provisions of the Act after arriving at the gross total income. The deductions mentioned in the sections in Chapter

VIA are to be allowed for the purpose of finding out the total income of an assessee. No deductions are to be made under any of these sections

included in Chapter VIA at the time of computation of the total income. Section 80I, clause (i) provided as follows :

The company to which this section applies, where the gross total income includes any profits and gains attributable to any priority industry, there

shall be allowed, in accordance with and subject to the provisions of this section, a deduction from such profits and gains of an amount equal to

eight per sent thereof, in computing the total income of the company.

6. There is no dispute in this case that only such amount of the profits and gains attributable to any priority industry which has been included in the

gross profit will qualify for exemption u/s 80I. The only dispute, however, is how to compute "profits and gains attributable to any priority

industry".

7. It is the contention of the revenue that profits and gains of priority industry must be profits and gains after deduction of all expenditures. This

proposition cannot be disputed. There are many expenditures of the company which are not only in respect of priority industry but also in respect

of other industries under the management of the company. One of such expenditures is the payment made to the managing agents. The revenue''s

contention is that the proportionate income of the managing agency by way of commission must be deducted from the profits of the priority

industry to find out the profits and gains of priority industry for the purpose of computation of relief u/s 80I. That raises the question : What is the

profit and gain attributable to any priority industry ?

8. In this connection the two judgments of the Supreme Court on which reliance has been placed by the Tribunal are instructive. The first judgment

is in the case of Commissioner of Income Tax, Bombay Vs. C Parakh and Co. (India) Ltd., . This judgment relates to deducibility of commission

of a portion of the managing agency commission from the business carried on by the assessee, inter alia, in Pakistan for the purpose of computation

of profits in Pakistan. There the assessee carried on some business at a number of places. The net profits of the business had to be ascertained by

putting together the profits of all the branches and deducting therefrom all the expenses. The fact that some of the branches were in foreign

territories did not make any difference to the position because the assessee was "an ordinary resident within the taxable territories''. The Supreme

Court held that whether the assessee was entitled to a particular deduction or not would depend on the provisions of law relating thereto and not

on the view which the assessee might take of its rights. In that case the assessee- company had its head office at Bombay and maintained a branch

office at Karachi for purchasing cotton for shipment to Bombay or for export direct to other places. The managing agents of the assessee-company

were entitled to a remuneration of 20 per cent of the net annual profits of the assessee-company. The assessee had apportioned the managing

agency commission and debited the proportionate amount in the respective profits and loss accounts for the Bombay head office and the Karachi

Branch. In computing the Pakistani income of the assessee for the purpose of double taxation relief, the ITO deducted from the income of the

Karachi Branch the proportionate managing agency commission. The AAC confirmed the order. But the Tribunal and the High Court on a

reference held that the managing agency commission in its entirety should be debited to the Bombay Branch. It was held by the Supreme Court

that the profits earned in India and Karachi were to be thrown together and the expenses including the managing agency commission deducted

therefrom and, therefore, the assessee-company was entitled to deduct the entire commission against the Indian profits. The Supreme Court further

held that the appropriation of the proportionate commission in respect of profit earned at Karachi was not in accordance with the agreement or

with the rights of the assessee under the law. It was observed by Venkatarama, J. :

Under that agreement, the managing agents are entitled to a 20 per cent commission on the annual net profits of the company, and to ascertain

those profits, one has to take into account the result of the trade in all its branches. In the present case, profits were earned during the accounting

period both in Bombay and in Karachi, and the apportionment of the commission between the two branches makes no material difference in the

result. But it might happen that the business at Bombay results in profit, while that at Karachi ends in loss. In that event, what the managing agents

would be entitled to would be commission not on the profits made in Bombay but on the net profits after setting off the loss in the Karachi Branch

against the profits of the Bombay business. And that would also be the position if the business at Bombay resulted in loss, while that at Karachi

ended in profit. The appropriation, therefor of Rs. 1,23,719 as proportionate commission in respect of the profits of Rs. 6,18,599 earned at

Karachi in the profit and loss statement for that branch is not in accordance either with the terms of the managing agency agreement, or with the

rights of the respondent under the law."" (p. 666)

9. In the case of Commissioner of Income Tax, Bombay Vs. Maharashtra Sugar Mills Ltd., Bombay, the assessee-company owned extensive

lands on which it grew sugarcane and used the sugarcane for manufacture of sugar in its factory. The Tribunal found that the cultivation of

sugarcane and the manufacture of sugar by the assessee constituted one single and indivisible business. The question was whether a part of the

managing agency commission paid by the company could be allowed on the ground that the part related to the management of sugarcane

cultivation income from which was exempted from tax as agricultural income. It was held by the Supreme Court that the entire managing agency

commission was laid out or expended for the purpose of business carried on by the assessee and was allowable u/s 10(2)(xv) of the Indian

Income- tax Act, 1922. The fact that the income from a part of the business was not exigible to tax under the Act was not a relevant circumstance.

The Supreme Court pointed out that equitable consideration was wholly out of place in construing the provisions of a taxing statute. If the

allowance claimed is permissible under the Act, then the same has to be deducted from the profits.

10. The principles laid down by the Supreme Court in the aforesaid cases clearly apply to the facts of the instant case. It is not the case of the

revenue that various units of business carried on by the assessee independently are separate business concerns. The assessee had relied on the

aforesaid judgments of the Supreme Court before the Tribunal. No attempt was made to distinguish these judgments on the ground that the

business carried on by the assessee were separate and independent transactions.

11. In view of the principles laid down by the Supreme Court in the aforesaid two judgments, both the questions are answered in the negative and

in favour of the assessee. There will be no order as to costs.

Bhagabatiprasad Banerjee, J.

I agree.