

(1994) 11 BOM CK 0059

Bombay High Court**Case No:** Income-tax Reference No. 112 of 1983

Commissioner of Income Tax

APPELLANT

Vs

Amritlal and Co. Ltd.

RESPONDENT

Date of Decision: Nov. 9, 1994**Acts Referred:**

- Income Tax Act, 1961 - Section 104, 104(1), 105, 106, 107

Citation: (1995) 125 CTR 323 : (1995) 212 ITR 540**Hon'ble Judges:** S.M. Jhunjhunwala, J; B.P. Saraf, J**Bench:** Division Bench**Advocate:** G.S. Jetley, for the Appellant;

Judgement

Dr. B.P. Saraf, J.

By this reference u/s 256(1) of the Income Tax Act, 1961, the Income Tax Appellate Tribunal has referred the following question of law to this court for opinion at the instance of the Revenue :

"Whether, on the facts and in the circumstances of the case in considering whether the provisions of section 104(1) apply in the case of the company as an investment company, the Tribunal was right in law in taking an overall view of the functioning of the company instead of confining its attention to the definition of investment company as contained in section 109(ii) for the assessment year 1972-73 ?"

2. The assessee is a company in which the public are not substantially interested. During the assessment year 1972-73 relevant to the previous year ending March 31, 1972, the assessee-company was dealing in dyes and chemicals manufactured by others. Apart from the business income from this source, it had also income from dividends, income from subletting of premises and property income. In addition to this, it had also earned long-term capital gains on sale of certain shares held by it as investment. The gross income of the assessee for the above assessment year stood as below :

3. Out of the above income of Rs. 19,66,789, a sum of Rs. 10,67,474 happened to form the income from house property, other sources and capital gains. The Income Tax Officer held the company to be an investment company within the meaning of section 109(ii) of the Income Tax Act, 1961, on the basis that the income from these sources was more than 50 per cent. of its gross total income. He, therefore, estimated the net distributable income of the assessee-company for the year at Rs. 8,93,503 and the amount to be distributed as dividends at Rs. 8,04,153. As against this, the assessee-company actually distributed a dividend of only Rs. 4,80,000. Thus there was a shortfall of Rs. 3,24,153 in the distribution of dividends. The Income Tax Officer, therefore, levied additional tax of Rs. 2,06,752 u/s 104(1) of the Act. The assessee appealed to the Commissioner of Income Tax (Appeals). The Commissioner accepted the contention of the assessee that it was not an investment company and deleted the additional tax levied by the Income Tax Officer. The appeal of the Revenue against the order of the Commissioner (Appeals) was rejected by the Income Tax Appellate Tribunal ("the Tribunal"). Hence, this reference at the instance of the Revenue.

4. Mr. Jetley, learned counsel for the Revenue, submits that the total income from the sources specified in clause (ii) of section 109 of the Act being more than 50 per cent. of the gross total income of the assessee-company, the Income Tax Officer was justified in holding that it was an investment company and the Commissioner (Appeals) and the Tribunal were not correct in reversing the same and holding it to be not an investment company by taking an overall assessment of the activities of the company during the year under consideration as well as last number of years.

5. Section 104 of the Act provides for the levy of additional tax on undistributed income of certain companies. This section, so far as is relevant, at the material time read as under :

"104. Income Tax on undistributed income of certain companies. - (1) Subject to the provisions of this section and of sections 105, 106, 107 and 107A, where the Income Tax officer is satisfied that in respect of any previous year the profits and gains distributed as dividends by any company within the twelve months immediately following the expiry of that previous year are less than the statutory percentage of the distributable income of the company of that previous year, the Income Tax Officer shall make an order in writing that the company shall, apart from the sum determined as payable by it on the basis of the assessment u/s 143 or section 144, be liable to pay Income Tax at the rate of -

(a) fifty per cent., in the case of an investment company.

(b) thirty-seven per cent., in the case of a trading company, and

(c) twenty-five per cent., in the case of any other company, on the distributable income as reduced by the amount of dividends actually distributed, if any, within the said period of twelve months."

6. The expressions, "distributable income" and "statutory percentage" are defined, respectively, in clauses (i) and (iii) of section 109. These clauses, so far as relevant, read :

"(i) "distributable income" means the gross total income of a company as reduced by -

(a) the amount of Income Tax payable by the company in respect of its total income, but excluding the amount of any Income Tax payable u/s 104;.....

(iii) "statutory percentage" means, -

Explanation. - The provisions of this Chapter shall, in relation the remaining part of the gross total income aforesaid, apply as if such part were the gross total income of the company; and, for the purpose of section 104, the amount of dividends actually distributed shall be deemed to be such proportion thereof as the part aforesaid bears to the gross total income of the company."

7. Thus the additional tax leviable u/s 104 is 50 per cent. of the undistributed balance of the distributable income in the case of an investment company, thirty-seven per cent. in case of a trading company and twenty-five per cent. in case of any other company. The statutory percentage is also higher for investment companies than other companies. "Investment company" and "trading company" have been defined in clause (ii) and (iia) of section 109 of the Act. At the material time, these clauses read as under :

"109. "Distributable income," "investment company" and "statutory percentage" defined. - For the purposes of sections 104, 105 and 107A and this section, -

(ii) "investment company" means a company whose gross total income consists mainly of income which is chargeable under the heads "Interest on securities," "Income from house property", "Capital gains" and "Income from other sources";

(iia) "trading company" means a company whose business consists mainly in dealing in goods or merchandise manufactured, produced or processed by a person other than that company and whose income attributable to such business included in its gross total income is not less than fifty-one per cent. of the amount of such gross total income;"

8. From the definition of investment company set out above, it is evident that a company can be held to be an investment company only if its gross total income consists mainly of income which is chargeable under the heads specified therein. It is not the actual income arising in a particular year under those heads vis-a-vis income falling under other heads that is determinative of the real character of a company. The decisive factor is the nature of the activities of the company which give rise to the income. A company engaged mainly in business or industrial activities cannot be held to be an investment company merely because in

a particular year its income from such business or industrial activity is insignificant or a negative figure and most of the income of that year turns out to be income from investment, income from securities, capital gains, etc. The definition nowhere says that if "in any assessment year" the income of the assessee which is chargeable under any of the heads specified in clause (ii) is not less than 51 per cent. of the amount of its gross total income, it will have to be treated as "investment company" for that assessment year. Had that been intent, the Legislature would have said so in specific terms as has been done in the Explanation to sub-section (4) of section 104 of the Act (as it stood at the material time) which provides that for the purposes of clause (a) thereof "the business of a company shall be deemed to consist mainly in the construction of ships or in the manufacture or processing of goods, etc., if the income attributable to any of these activities included in the gross total income of the relevant previous year is not less than fifty-one per cent. of such income." There is no such deeming provision in the definition of investment company.

9. Again, a trading company has been defined in clause (iia) to mean a company "whose business consist mainly in dealing in goods or merchandise and whose income attributable to such business included in its gross total income is not less than fifty-one per cent. of the amount of such gross total income". Thus a company whose business consists mainly in dealing in goods or merchandise would still not be treated as a trading company for the purposes of section 104 of the Act if its income attributable to such business is not less than fifty-one per cent. of the amount to its gross total income. In that event, it will be treated as "any other company" and additional Income Tax u/s 104 of the Act would be leviable at the rates applicable to such company.

10. Thus, in order to term a company an "investment company" its gross total income should consist "mainly" of income from securities, house property, capital gains, etc. The expression "mainly" appearing in the definition of investment company in clause (ii) means "substantially" or "primarily". If the business of the company consists mainly in dealing in goods or merchandise, it cannot be held to be an "investment company" within the meaning of clause (ii) merely because, for one reason or the others, its income from business happens to fall short of its income from investments, etc. in a particular previous year. The decisive factor for determining whether a company is an "investment company" or any other company is, therefore, the true nature of the primary activities of the company. If the activities of the company are such that its total gross income "mainly" consists of income from securities, etc., it would be termed an investment company. The word "mainly" is somewhat akin to "wholly" and has been used to mean the whole or a substantial portion of the total gross income of the assessee. It cannot be construed to mean "not less that fifty-one per cent."

11. In the instant case, the uncontroverted factual position is that the assessee is a dealer in dyes and chemicals manufactured by others and derives income

therefrom. In addition to that, the assessee also derives income from dividends, sub-letting of premises and properties. In the previous year relevant to the assessment year 1972-73 to which this relates, the assessee derived income also by way of long-term capital gains. The business income of the assessee during this year was Rs. 8,99,324 as against income of Rs. 10,66,798 from house property, other sources and capital gains. The income from sources specified in clause (ii) of section 109, thus being more than fifty per cent. of the total gross income for that year, the Income Tax Officer held the assessee to be an investment company. On appeal, the Commissioner of Income Tax (Appeals) did not approve of the above approach of the Income Tax Officer. He was of the opinion that on a reading of the definition of "investment company" in clause (ii) of section 109 of the Act, it would not be proper to hold the assessee to be an investment company only because in one, two or three years its income from business fell short of fifty per cent. of the gross total income. According to him, to determine whether a company's income "mainly" comprised income from house property, etc., it was necessary to take a broad view of the pattern of the income of the company, wherein the relative significance of the business and non-business income over a fairly long period had to be taken into account. He, therefore, considered the particulars of income of the assessee from the assessment years 1951-51 to 1977-78 which showed that in all these years except in the assessment years 1968-69, 1969-70, 1971-72 and 1972-73, the assessee's income from business always far exceeded its non-business income. The Commissioner also perused the memorandum and articles of association of the assessee-company and held that the assessee was not an investment company. The Tribunal upheld the above order of the Commissioner (Appeals).

12. We have carefully considered the above facts. The assessee's income from business was above 90 per cent. of its total gross income during the previous years relevant to the assessment years 1951-52 to 1959-60. It was over 78, 62, 75, 50 and 68 per cent. of the total income in the next five years. It was, however, 10.92 per cent. and 15.19 per cent. in the previous years relevant to the assessment years 1968-69 and 1969-70. It was over 50 per cent. in the previous year relevant to the assessment years 1970-71. It again fell short of 50 per cent. in the assessment years 1971-72 and 1972-73 when it was 44.46 and 45.73 per cent. of the total income, respectively. Therefore, it always far exceeded fifty per cent. It was over 69, 70, 71 and 65 per cent. in the assessment years 1973-74, 1974-75, 1975-76 and 1977-78. Thus in a period of 27 years, only in four year including the assessment year under consideration the business income of the assessee fell short of fifty per cent. of its total gross income.

13. The memorandum of association and articles of association of the assessee-company also clearly go to show that it was formed with the object of carrying various types of business. The purchase of land, building, etc., and letting out the same was only for furtherance of the above object. Factually also the assessee-company's business consisted mainly in dealing in dyes and chemicals

manufactured by others and it derived its income mainly from the said activity. During the twenty-seven years of its existence, it was only in four years including the year under consideration that, due to one reason or the other, its income from business fell short of fifty-one per cent. of its total income. The question that arise for consideration is whether merely on that account, it can be held to be an "investment company" within the meaning of clause (ii) of section 109 of the Act. The answer in clear terms has to be in the negative. Because from a perusal of the activities of the company and its income pattern since 1950-51, it is evident that its gross total income mainly consists of income from business and not income from securities, house property, capital gains and other sources. The company is, therefore, not an investment company. It cannot be held to be so in a particular year merely because its income from non-business sources specified in clause (ii) of section 109 in that year happens to exceed its business income.

14. We are, therefore, of the clear opinion that under the facts and circumstances of the case, the Tribunal was justified in taking an overall view of the functioning of the company instead of confining its attention to the income of the year under consideration for the purpose of determining whether the assessee-company was an "investment company" within the meaning of clause (ii) of section 109 of the Act and on a consideration of the same in holding that it was not an investment company.

15. In the premises, the question referred to us is answered in the affirmative and in favour of the assessee.

16. Under the facts and circumstances of the case, there shall be no order as to costs.