Commissioner Of Income-Tax Bombay vs Maharashtra Sugar Mills Ltd. Bombay on 16 August, 1971

Equivalent citations: 1971 AIR 2434, 1972 SCR (1) 202, AIR 1971 SUPREME COURT 2434, 1971 TAX. L. R. 1405

Author: K.S. Hegde

Bench: K.S. Hegde, A.N. Grover

PETITIONER:
COMMISSIONER OF INCOME-TAX BOMBAY

Vs.

RESPONDENT:
MAHARASHTRA SUGAR MILLS LTD. BOMBAY

DATE OF JUDGMENT16/08/1971

BENCH:
HEGDE, K.S.
BENCH:
HEGDE, K.S.
GROVER, A.N.

CITATION:
1971 AIR 2434 1972 SCR (1) 202

ACT:
Income-tax Act (11 of 1922), s. 10(2)(xv) and r. 23 of Rules --Part of assessee's income not exigible to tax-Commission to managing agent-Whether part of commission relating to such income not deductible from assessee's gross profits.

HEADNOTE:
The assessee was a limited company. it owned extensive lands in which sugar cane was grown and the cane was used by the assessee for the manufacture of sugar in its factory. The cultivation of sugar cane and the manufacture of sugar by the assessee constituted one single and indivisible business. In the assessment year 1957:58, the assessee claimed deduction of remuneration paid to its managing agents under s.10(2)(xv) of the Indian Income-tax Act, 1922, as an item of expenditure laid out or expended wholly or exclusively for the purpose of its business. The Income-tax

Officer and the Appellate Assistant Commissioner disallowed a part of the remuneration on the grounds that part of the assessee's business namely cultivation of sugar cane, being an agricultural operation, the income therefrom was not exigible to tax, and therefore, any expenditure incurred in respect of that activity was not deductible. The Tribunal and the High Court on reference, however, upheld the plea of the assessee that the entire sum was deductible.

Dismissing the appeal to this Court,

HELD: (1) The mandate of s. 10(2)(xv) is plain and unambiguous. To find out whether a deduction claimed is permissible under the Act or not, all that the Court has to do is to examine the relevant provisions of the Act. Equitable considerations are wholly out of the place in construing the provisions of the taxing statute. If the allowance claimed is permissible under the Act then it has to be deducted from the grow profits, and if it is not so permissible it has to be rejected. [232 H; 233 A-D]

In the. present case, the allowance claimed was undoubtedly laid out or expended for the purpose of the business carried on by assessee. The fact that income arising from a part of that business was not exigible to tax under the Act was not a relevant circumstance. [233 D-E]

C.I.T., Bombay v. Parakh and (India) Ltd., 29 I.T.R., 661, and C.L T. Madras v. Indian Bank Ltd., 56 I.T.R. 79, followed.

S.A.S.S. Chellappa Chettiar v. C.I.T, Madras, 5 I.T.R., 97 and Salt & Industries Agencies Ltd. Bombay v. C.LT., Bombay City, 18 I.T.R. 58, referred to.

(2) Rule 23 of the rules framed under the Income-tax Act says that in computing the taxable income of a business the agricultural income as defined in s. 2 of the Act should be deducted from the tota

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income for arriving at the taxable income. The rule further says that No further deduction shall be made of any expenditure incurred by the assessee as cultivator or receiver of rent in kind'. If the rule is read with s. 2(1) it is clear that reference to the expenditure incurred by the assessee as a cultivator only applies to the process ordinarily employed by a cultivator in raising the crops and all other incidental and supple mentary activities up to the stage of sale of the produce, and has nothing to do with disbursements such as payment of managing agency commission. [238E-H; 24OA-B]

JUDGMENT:

CIVIL APPELLATE JURISDICTION : Civil Appeal No. 1658 of 1968.

Appeal by special leave from the judgment and order dated September 22, 1967 of the Bombay High Court in Income-tax Reference No. 83 of 1962.

B. D. Sharma, and R. N. Sachthey, for the appellant V. Rajagopal, M. M. Vakil, B. Datta, J. B. Dadachanji, O. C. Mathur and Ravinder Narain, for the respondent. The Judgment of the Court was delivered by Hegde, J. This is an appeal by special leave. It arises from the decision of the Bombay High Court in Income-tax Reference No. 83 of 1962 on its file. That Reference was made by the Income-tax Appellate Tribunal, Bench 'B', Bombay. The question of law which was referred for the. opinion of the High Court under s.66(1) of the Indian Income-tax Act, 1922 (to be hereinafter referred to as the Act) is:

> "Whether on the facts and in the circumstances
>
> -of this case the Department could disallow a sum of Rs. 1,26,359/- a portion of the managing agency ,commission paid by the assessee company for the ,assessment year 1957-58 in computing the income from business of the assessee company."

The assessee is M/s. Maharashtra Sugar Mills Ltd. The concerned assessment year is 1957-58, the corresponding account year ending on 30-9-1956. , The assessee is a Limited Company. it carries on business of manufacture of sugar from.sugar cane. It owns extensive lands in which sugar cane is grown. The sugar cane grown in these lands is used by the assessee for manufacture of sugar in its factory. The finding of the Tribunal is that 16-M 1245 Sup. Cl/71 the cultivation of sugar cane and the manufacture of sugar by the assessee constitute one single and indivisible business. The assessee company is managed by managing agents. The managing agents were paid remuneration in accordance with the agreement entered into between the assessee company and the managing agents; The managing agents's commission roughly worked out at 10 percent of the profits of the company. In the assessment year in question the managing agents were entitled to a commission of Rs. 4,86,228 /6 /-. In its assessment proceedings, the assessee claimed deduction of this sum under s.10(2)(15) as an item of expenditure laid out or expended wholly or exclusively for the purpose of its business. Out of that sum, the Income-tax Officer disallowed a sum of Rs. 1,26,359/- on the ground that the same relates to the commission of the managing agents for managing the sugar cane cultivation part of the business. In appeal, the Appellate Assistant Commissioner concurred with the view taken by the Income-tax Officer. The assessee took up the matter in second appeal to the Income-tax Appellate Tribunal. The Tribunal upheld the plea of the assessee that the entire sum is deductible under S. 10(2) (15). It also rejected the contention of the department that on the facts of the case rule 23 of the Rules framed under the Act is applicable. In the Reference

-referred to earlier, the High Court agreeing with the view. taken by the Tribunal answered the question in favour of the assessee. Hence this appeal.

The finding of the Tribunal that the cultivation of sugar cane as well as the manufacture of sugar constitutes one business is a finding of fact. That finding has not been challenged before us What. was urged on behalf of the department is that the assessee's business consisted of two parts namely (1) cultivation of sugar cane and the manufacture of sugar. The former part being agricultural

operation, the income therefrom is not exigible to tax and therefore any expenditure incurred in respect of that activity is not deductable. This contention proceeds on the basis that only expenditure incurred in respect of a business activity giving rise to income, profit or gains taxable under the Act can be given deduction to and not otherwise. We see no basis for this contention. To find out whether a deduction claimed is permissible under the Act or not, all that we have to do is to examine the relevant provisions of the Act. Equitable considerations are wholly out of place in construing the provisions of a taxing statute. We have to take the provisions of the statute as they stand. If the allowance claimed is permissible under the Act then the same has to be deducted from the gross profit. If it is not permissible under the Act, it has to be rejected. As men- tioned earlier, it is not disputed that the cultivation of sugar cane and the manufacture of sugar constituted one single and indivisible business. Section 10(2) says that profits under S. 10(1) in respect of a business should be computed after deducting the allowances mentioned therein. One of the allowances allowed is that mentioned in s.10(2)

(xv) which says that any expenditure laid out or expended wholly and exclusively for the purpose of such business shall be deducted as an allowance. The mandate of s 10 (2)(15) is plain and unambiguous. Undoubtedly the allowance claimed in this case was laid out or expended for the purpose of the business carried on by the assessee. The fact that the income arising from a part of that business is not exigible to tax under the Act is not a relevant circum- stance. For the foregoing reasons we agree with the view taken by the High Court.

Turning now to the decided cases, we shall first refer to the decision of the Madras High Court in S. A. S.S. Chellappa Chettiar v. Commissioner of Income-tax, Madras(1) The facts of that case are, : The assessee was carrying on the business of money lending in Burma. For the purpose of that business he was borrowing money from others at a lower rate of interest and advancing loans to his-constituents at a higher rate. In the course of his business, he was obliged to receive agricultural lands in repayment of his debts from some of his constituents. In his assessment proceedings he claimed deduction of the interest David by him in respect of his borrowings. Part of the money borrowed by him had been advanced to constituents who, as mentioned earlier, had made over their agricultural lands to the assessee. The question arose whether the interest paid in respect of the money advanced to those constituents was deductable in computing the profits and gains of the assessee. The High Court held that he was entitled to the deduction claimed and further he was also entitled to deduction in (1) 5 I.T. P,. 97.

respect of the establishment and other charges incurred by him for managing and cultivating such lands and the amount spent for obtaining conveyances of such lands. Sir H. O. C. Beasley C. J., speaking for the Court observed:

> "It seems to us that the governing section in order to decide this matter must be Sec. 10(2)(iii). Was the capital borrowed for the purpose of the assessee's business ? No difficulty arises about that, for it is ,conceded that it was so borrowed. It was also unquestionably used for the purpose of the business because it is again conceded that it was lent to the borrowers. Does it continue to be so used ? It is in that respect that it is important again to emphasise that this case has been argued, before us on the

> basis that these lands came into and were retained in the possession of the assessee in payment of a moneylending debt and ex- necessitate."

The test applied by the learned Chief Justice appears to us to be the correct one.

We shall next take up the decision of the Bombay High Court in Salt and Industries Agencies Ltd., Bombay v. Commissioner of Income-tax, Bombay City (1). The assessee in that case was a company incorporated in Bombay. They were the managing agents of another company which was also incorporated in Bombay. The managed company had business both in British India as well as in the Indian States. The profits arising from the business activities of the managed company in the Indian States was not exigible to tax but yet the assessee claimed that a part of the commission earned by it being in respect of business carried on outside British India, the same could not be considered as an income earned in British India. That contention was rejected by the High Court. In the course of its judgment, the High Court observed:

> "It is perfectly true that as far as the parent company is concerned, the profits made at Kandla could be said to have arisen and accrued at Kandla, but as far as the managing agents are concerned, their commission has nothing whatever to do with those profits. (1) 18 L.T.R. 58.

Their commission is only concerned with the ultimate determination of all the workings of the company and the finding out whether and what profits has been earned by the company. It cannot be said that as profits were earned by the parent company, the commission also was accruing or arising to the managing agents." - In Commissioner of Income-tax, Bombay v. C Parakh & Co. (India) Ltd. I. The ratio of that decision bears on the question of law that we are considering. The assessee company therein was resident and ordinarily resident in India. It had its head office in Bombay. It maintained a branch at Karachi for purchasing cotton for shipment to Bombay or to export direct to other places.' By an agree- ment, the managing agents of the assessee company were entitled to a remuneration of 20 percent of the annual net profits of the assessee company to ascertain which the result of the trade in all its branches had to be taken into account. The assessee apportioned the managing agency commission and debited the proportionate amount in the respective profit and loss account for the Bombay head office and the Karachi branch. In computing the Pakistan income of the assessee for the purpose of double taxation relief the Income-tax Officer deducted from the income of the Karachi branch the proportionate managing agency commission. The Appellate Assistant Commissioner confirmed that 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. On appeal this Court held that the entire managing agency commission was liable to be debited against the Indian profits and further assessee company could not be estopped from claiming the benefit of such deduction by reason: of the fact that it erroneously allocated a part of it toward the profits earned in Karachi. In the course of; its judgment this Court observed:

> "Section 10(2)(xv) of the Indian Income-tax Act provides that in computing the profits of a business allowance is to be made for any expenditure laid out or expended wholly and exclusively for the purpose of such business.. Now the respondent is

carrying on (1) 29 I.T.R. 661.

business in cotton both in India and in Karachi. When an assessee carries on the same business at a number of places there is for the purpose of section 10 ,only one business and the net profits of the business have to be ascertained by pooling together the profits ,earned in all the, branches and deducting therefrom all the expenses. The fact that some of the branches are in foreign territories will make no difference in the position if the assessee is as in the present case resident and ordinarily resident within the taxable territories. Therefore the profits earned in India and in Karachi have to be thrown together and the expenses including the commission payable to the managing agents deducted therefrom and it is the net profits thus struck that become chargeable under the Act. That is how the Income-tax Officer has worked out the figures. The respondent is therefore clearly entitled to a deduction of the whole of the commission of Rs. 3,12,699 paid to the managing agents including the sum of Rs. 1,23,719 against the Indian profits." Lastly we refer to the decision of this Court in Co mission of Income-tax Madras v. Indian Bank Ltd(1). Therein the respondent, a banking company, in the course of its business, invested a large sum in securities, including securities the interest on which was exempt from tax. Profits and losses on the purchase and sale of such securities were duly taken into account in computing the business income of the respondent. The% question for decision was whether the interest paid by the respondent on the amount invested in securities, whose interest was tax free, was deductable from its gross profits. This Court held that interest paid by the respondent on moneys borrowed from its various depositors had to be allowed in its entirety under S. 10(2) (iii) of the Act and there was no warrant for disallowing a proportionate part of the interest referable to money borrowed for the purchase of securities whose interest was tax-free. In the course of the Judgment Subba Rao, J. (as he then was) observed:

> "In our opinion,, in construing the Act, we must adhere closely to the language of the Act. If there is ambiguity in the terms of a provision, recourse must (1) 56 I.T.R. 79.
>
> naturally be had to well-established principles of construction but it is not permissible first to create an artificial ambiguity and then try to resolve the ambiguity by resort to some general principle.

We are concerned with the interpretation of section, 10. Let us then look at the language employed. Sub-section (1) directs that an assessee be taxed in respect of the profits and gains of business carried on by him. What is the business of the assessee must first be looked at. Does he carry on one business or two businesses or along with the business carried on by him some activity which is/not a business ? If he is carrying on an activity which is not business, we must leave out of account the receipts of that activity. That is the first step. Secondly, we must look at section 10(2) and deduct all the allowances permission ale to him. In allowing a deduction which is permissible the question arises: Do we look behind the ,expenditure and see whether it has the quality of ,directly or indirectly producing taxable income ? 'The answer must be in the negative for two reasons: First, Parliament has not directed us to undertake this enquiry. There are no words in section 10(2) to that effect. On the other hand, indications are to the contrary. In Section 10(2)(xv), what Parliament requires to be ascertained is whether the expenditure has been laid out or expended wholly and

exclusively for the purpose of the business. The legislature stops short at directing that it be ascertained what was the purpose of the expenditure. If the answer is that ,it is for the purpose of the business, Parliament is not concerned to find out whether the expenditure has produced or will produce taxable income. Secondly, the reason may well- be that Parliament assumes that most types of expenditure which are laid out wholly and exclusively for the purpose of business would directly or indirectly produce taxable income, and it is not worth the administrative effort involved to go further and trace the expenditure to some taxable income."

On behalf of the department reliance was sought to be placed on the decision of this Court in Badridas Doga v.

Commissioner of Income-tax(1). The ratio of that decision does not bear on the issue arising for decision in this case. That decision is wholly irrelevant for our present purpose It was next urged on behalf of the department that in view of rule 23 of the Rules framed, it was permissible for the Income-tax Officer to split up the commission given to the managing agents. We see no merit in this contention. Rule 23 to the extent material for our present purpose reads:

> "23(1) In the case of Income which is partially agricultural income as defined in section 2 and partially income chargeable to income-tax under the head "business" in determining that part which is chargeable to income-tax the market value of any agricultural produce which has been raised by the assessee or received by him as rent in kind and which has been utilised as raw material in such business or the sale receipts of which are included in the accounts of the business shall be deducted, and no further deduction shall be made in respect of any expenditure incurred by the assessee as a cultivator or receiver of rent in kind."

Rule 23 lays down the method of computing the taxable income of a business which partly arises from the utilisation of agricultural produce as raw material in the business. It says that in computing the taxable income, agricultural income as defined in S. 2 of the Act should be deducted from the total income for arriving at the taxable income. For determining what the agricultural income is the Income-tax Officer must determine the market value of the agricultural produce used as raw material in the business. The rule further says that "no further deduction shall be made of any expenditure incurred by the assessee as a cultivator or receiver of rent in kind." (emphasis supplied). The managing agency commission given to the assesses is not an expenditure incurred by the assessee as a cultivator or as a receiver of the rent in kind. The last part of subrule (1) of Rule 23 merely stipulates that the expenditure incurred by the assessee for his agricultural operation or incurred by him as receiver of rent in kind is not to be deducted while arriving at the taxable income. Section (1) 34 I.T.R. 10.

2(1) of the Act defines agricultural income. That section reads:

> "agricultural income" means-

(a) any rent or revenue derived from land which is used for agricultural purposes, and is either assessed to land-revenue in the taxable territories or subject to a local rate assessed and collected by officers of the Government as such;

(b) any income derived from such land by-

(i) agricultural or

(ii) the performance by a cultivator or receiver of rent in kind of any process ordinarily employed by a. cultivator or receiver of rent-in-kind to render the produce raised or received by him fit to be taken to market, or

(iii) the sale by a cultivator or receiver of rent-in-kind of the produce raised or received by him, in respect of which no process has been performed other than a process of the nature described in sub-clause (ii).

(c) any income derived from any building owned and occupied by the receiver of the rent or revenue of any such land, or occupied by the cultivator, or the receiver of rent in kind, of any land with respect to , which, or the produce of which any operation mentioned in sub-clauses (ii) and (iii) of claus e (b) is carried on:

Provided that the building is on' or in the immediate vicinity of the land, and is a building which the receiver of the rent or revenue or the cultivator or the receiver of the rent-in-kind by reason of his connection with the land, requires as a dwelling house, or as a storehouse, or other out-building,"

If rule 23 is read along with S. 2(1), it is clear that Preference to, expenditure incurred by the assessee as a

-cultivator applies to the process ordinarily employed by,a cultivator in raising the crops and all other incidental and supplementary activities upto the stage of sale of the produce.' That rule has nothing to do with disbursements such as payment of managing agency commission. In the result this appeal fails and the same is dismissed with costs.

V.P.S. Appeal dismissed.