Shree Ram Mills Ltd., Bombay vs Commr. Of Excess Profits Tax, Central ... on 16 January, 1953

Equivalent citations: AIR1953SC485, [1953]23ITR120(SC), AIR 1953 SUPREME COURT 485

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Bench: N.H. Bhagwati

JUDGMENT

Bose, J.

1. This appeal comes from Bombay. It raises two questions under the Excess Profits Tax Act, 1940. The first concerns Rule 5 of schedule II of the Act and the other raises a question about the managing agency commission due to the managing agents of the assessee company.

2. The assessee is the Shree Ram Mills Limited of Bombay. The assessment year is 1945-46 and the accounting year is the calendar year 1944. The Income-tax Officer assessed the profits for income-tax at Rs. 46,18,384 and that is not questioned.

3. The Excess Profits Tax Officer computed the profits, for excess profits tax purposes, at Rs. 46,94,304. In reaching this figure he excluded certain items in the return for determining how the profits increased the capital; for example, he excluded money given away as presents and in charity etc.

4. Now in order to determine the quantum of excess profits tax payable by an assessee it is necessary under the Act to compute, among other things, the average amount of capital employed by the business during a certain period. This, under Section 2(3), has to be the average amount of capital "as computed in accordance with the second Schedule." That brings in the disputed rule, Rule No. 5 in Schedule II.

5. It runs as follows :-

> "For the purpose of ascertaining the average amount of capital employed in a business during any period, the profits or losses made in that period shall excepts so far as the contrary is shown, be deemed -
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> (a) to have accrued at an even rate throughout the period; and

> (b) to have resulted, as they accrued, in a corresponding increase or decrease, as the case may be, in the capital employed in the business."

6. The dispute centers round the words we have underlined. The learned counsel for the assessee contends that the words only govern clause (a) and not clause (b). The department has accepted in this case that the profits accrued at an even rate because the assessee has not rebutted that presumption nor has the department attempted to do so. The learned counsel for the assessee contends that that being so, the department is bound to apply clause (b) because the words we have underlined only govern clause (a) and not clause (b). His contention is that Rule 5 is an artificial rule which creates a fiction, namely that the profits accrue evenly over the year even when that is not the fact. Therefore the moment either party shows that this is not the case Rule 5 falls to the ground as a whole because the artificial presumption it created has been rebutted. Clause (b), he contends, cannot have any independent existence because it is a mere corollary to clause (a). In the same way, he says, if clause (a) is accepted, then clause (b) lives also, and as clause (a) has been accepted here clause (b) must also be applied without anything more.

7. We do not agree. The word "deemed" clearly governs both clauses, for the fiction which the Rule creates is not only that the profits shall be deemed to have accrued at an even rate throughout the period, but further that they must be deemed to have resulted, as they accrued, in a corresponding increase or decrease in the capital. In the same way, the words "except so far as the contrary is shown" govern both clauses and it is open to either side to rebut the artificial presumptions created by that Rule by showing that either clause does not represent the true facts. Thus, it can be shown either that the profits did not accrue at an even rate throughout the period or that the profits did not actually go to increase the capital, as for example when it was taken out of the business and handed over to charities and so forth, and if only one of the two presumptions is rebutted, the other stands.

8. The High Court resettled the first question we are asked to answer as follows :-

> "Whether on a true construction of Rule 5 of Schedule II of the Excess Profits Tax Act the expression 'so far as the contrary is shown' applies only to sub-clause (a) or also to sub-clause (b) ?"

9. We agree with the answer given by the High Court, namely that the words "so far as the contrary is shown" apply to both clauses (a) and (b).

10. The next question is about the managing agency commission. Under the Articles of Agreement entered into between the assessee and its managing agents the agents were to be paid a certain commission and the articles provided :-

> "The said commission shall be due to the said firm yearly on the thirty-first day of December in each and every year during the continuance of this agreement and shall be payable and be paid immediately after annual accounts of the said company have been passed by the shareholders of the company....."

11. The managing agents left the commission lying with the assessee. The assessee contends that this constitutes a "borrowing" within the meaning of Rule 2A of Schedule II. The Commissioner of Income-tax says it is a "debt" within the meaning of Rule 2. We agree with the High Court that this is a "debt" and not a "borrowing".

12. At bottom this is a question of fact. Of course, money so, left could, by a proper agreement between the parties, be converted into a loan, but in the absence of an agreement mere inaction on the part of the managing agents cannot convert the money due to them, and not withdrawn, into a loan. A loan imports a positive act of lending coupled with an acceptance by the other side of the money as a loan. The relationship of borrower and lender cannot ordinarily come about by mere inaction. The clause in the Articles of Agreement quoted above was relied on for the purpose of showing that there was such an agreement in the case. We are unable to construe the provisions in that way. They merely give the managing agents a right to receive their commission at a certain time. If the money is not paid in time it lies with the assessee as a debt due to the agents.

13. The second question was framed as follows :-

> "Whether the managing agency commission payable by the company to its managing agents for the year 1943 is borrowed money for the purposes of Rule 2A or a debt for the purposes of Rule 2 of Schedule II to the Excess Profits Tax Act ?"

14. We agree with the High Court that it is a debt under Rule 2 and not a borrowing under Rule 2A.

15. The result is that the appeal fails and is dismissed with costs.

16. Appeal dismissed.