M/S. Karamchand Premchand Pvt. Ltd. ... vs The Commissioner Of Income-Tax, ... on 1 December, 1992

Equivalent citations: AIR1993SC1613, [1993]200ITR268(SC), 1992(3)SCALE266, (1993)1SCC624, AIR 1993 SUPREME COURT 1613, 1993 (1) SCC 624, 1993 AIR SCW 332, 1993 TAX. L. R. 159, (1993) 67 TAXMAN 537, (1993) 200 ITR 268

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Bench: S.C. Agrawal, B.P. Jeevan Reddy

ORDER

B.P. Jeevan Reddy, J.

1. These two appeals one by the Assessee (Civil Appeal No. 2231 of 1977) and the other by the Revenue (Civil Appeal No. 2143 (NT) of 1977) arc preferred against the judgment of the Gujarat High Court in Income Tax Reference No. 4/73. The matter arises under the Companies (Profits) Surtax Act, 1964. It relates to computation of the capital is of the assessee-company. The assessment year is 1964-65.

2. Four questions were referred by the Income-tax Appellate Tribunal, Ahmedabad under Section 256(1) of the Act, two at the instance of the assessee and two at the instance of the revenue. The questions referred at the instance of the assessee are:

> (1) Whether on the facts and in the circumstances of the case, the Tribunal was justified in holding that there was a mistake apparent from the record in its order dated 1.7.1971 and in passing its miscellaneous order dated 15.2.1972?
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> (2) If the answer to the Question No. (1) is in positive, whether on the facts and in the circumstances of the case, the Tribunal was justified in directing that the following amount should be excluded in computing the capital of the company under the provisions of Rule 1 of the Second Schedule of the Companies (Profits) Sur-tax Act, 1964:-
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> i) Amount set apart for contingent liability. Rs. 4,50,000 ii) Amount set apart for proposed dividend. Rs. 15,82,000 iii) Provision for profit snaring bonus. Rs. 6,99,913

iv) Provision for pension Scheme. Rs. 50,000

3. The two questions referred at the instance of the Revenue which may be numbered as 3 and 4, are:

> (3) "If the answer to question No. (1) is in the negative then whether on the facts and in the circumstances of the case the Tribunal was right in holding that the above items indicated in question No. 2 should be included in the computation of the assessee's capital for the purpose of Companies (Profits) Sur-tax Act, 1964?
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> (4) "Whether on the facts and in the circumstances of the case, the Tribunal was right in holding that the amount of Rs. 9,97,410/- being credit to depreciation fund in excess of the amount actually allowed in income-tax assessment was a reserve in depreciation which should be included in the computation of the assessee's capital for the purposes of Companies (Profits) Sur-tax Act, 1964?

4. The assessee is a Private Limited Company known as Karamchand Premchand Private Limited. Ahmedabad which was subsequently renamed as Shahibaug Enterpreneures Private Limited, Ahmedabad. For, the assessment year 1964-65, the assessee filed a return under the Act for the period ending 31.3.1964 disclosing its chargeable profits at Rs. 67,001/-. The Income-tax Officer did not agree with the several claims made in the return. He determined the chargeable profits at Rs. 4,72,534/- and the net tax payable at Rs. 1,86,338.44p. An appeal preferred by the assessee was dismissed by the Appellate Assistant Commissioner of Super-Profit-Tax A-Range, Ahmedabad. The assessee then carried the matter to Income-tax Appellate Tribunal. By its order dated 1st July, 1971 the Tribunal allowed the appeal allowing several claims of the assesse. Soon thereafter, the revenue filed an application bringing to the notice of the Tribunal the Explanation appended to Rule in the Second Schedule to the Act. The Tribunal allowed the application on 15.2.1972. It held that several items which were treated by it as reserves in its order dated 1st July, 1971 could hot have been treated as such and that 5 they ought to have been treated as provisions. It is against the said order that the assessee as well the revenue both applied for referring certain questions of law for the opinion of the High Court.

5. The Companies (Profits) Sur-tax Act, 1964 was enacted by Parliament with a view to impose a special tax on the profits of certain companies. Section 4 contains the charging w provision. It says;

4. Charge of tax - Subject to the provisions contained in this Act, there shall be charged on every company for every assessment year commencing on arid from the 1st day of April, 1964, a tax (in this Act referred to as the surtax) in respect of so much of its chargeable profits of the previous year or previous years, as the case may be, as exceed the statutory is deduction, at the rate or rates specified in the Third Schedule.

6. The expression 'chargeable profits' is defined in Clause (5) of the section 2. According to it, 'chargeable profits' means "the total income of an assessee computed under the Income Tax Act, 1961 for any previous year or years as the case may be and adjusted in accordance with the

provisions of the First Schedule." The expression "statutory deduction" is defined in Clause-8 of Section 2. Omitting the provision which are not necessary for our purpose the definition reads as follows:

> statutory deduction" means an amount equal to ten per cent of the capital of the company as computed in accordance with the provisions of the Second Schedule, or an amount of two hundred thousand rupees, whichever is greater.

7. The Second Schedule contains the Rules for computing the capital of a company for the purposes of the Act. It would be appropriate to read the entire Rule-1 including the explanation at this stage.

1. Subject to the other provisions contained in this Schedule the capital of a company shall be the aggregate of the amounts, as on the first day of the previous year relevant to the assessment year, of-

> (i) its paid-up share capital;
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> (ii) its reserves, if any, created under the proviso (b) to Clause (vi-b) of Sub-section (2) of Section 10 of the Indian Income-tax Act, 1961 (XLIII of 1961);
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> (iii) its other reserves as reduced by the amounts credited to such reserves as have been allowed as a deduction in computing the income of the company for the purposes of the Indian Income-tax Act, 1922 (XI of 1922), or the Income-tax Act, (XLIII of 1961);
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> (iv) the debentures, if any, issued by it to the public;

Provided that according to the terms and conditions of issue of such debentures, they are not redeemable before the expiry of a period of seven years from the date of issue thereof; and

(v) any moneys borrowed by it from Government or the Industrial Finance Corporation of India or the Industrial Credit and Investment Corporation of India or any other financial institution which the Central Government may notify in this behalf in the Official Gazette or any banking institution (not being a financial institution notified as aforsaid) or any person in a country outside India:

> Provided that such moneys are borrowed for the creation of a capital asset in India and the agreement under which such moneys are borrowed provides for the repayment there of during a period of not less than seven years.
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> Explanation.-For the removal of doubts it is hereby declared that any amount standing to the credit of any account in the books of a company as on the first day of the previous year relevant to the assessment year which is of the nature of item (5) or item (6) or item (7) under the heading "RESERVES AND SURPLUS" or of any item under the heading "CURRENT LIABILITIES AND PROVISIONS" in the column relating to "Liabilities" in the "Form of Balance Sheet" given in Part I of Schedule VI

to the Companies Act, 1956 (I of 1956), shall not be regarded as reserve for the purposes of computation of the capital of a company under the provisions of this Schedule.

8. A reading of Rule-I shows that subject to the other provisions contained in the said Schedule, the capital of a company shall be the aggregate of the several amounts mentioned in the Rule as on the 1st day of the previous year relevant to the assessment year. The item which have to be so aggregated include the paid-up share capital, reserve mentioned in Clauses (ii) and (iii) debentures mentioned in Clause (iv) and the borrowed amounts mentioned in Clause (v). The Explanation appended to the Rule is clarificatory in nature. It refers to the form of balance-sheet given in part one of Schedule VI the Companies Act, 1956 and says that any is amount standing to the credit of any account in the books of a company (as on the first day of the previous year relevant to the assessment year) which is of the nature of item-5 or item-6 or item-7 under the heading "RESERVES AND SURPLUS" or of any item under the heading "CURRENT LIABILITIES AND PROVISIONS" in the column relating to liabilities shall not be regarded as reserves for the purposes of the Act.

9. The distinction between the reserves and provision has been dealt with exhaustively by this Court in Vazir Sultan Tobacco Company Limited etc. etc. V. Commissioner of Income-Tax, A.P. etc. etc. ., It indeed follows the principles enunciated in the earlier decisions of this Court in Metal Box Company of India Ltd. V. Their Workmen and CIT V. Century Spinning and Manufacturing Company Limited . Applying the principles flowing from the said decision, that the questions arising herein have to be answered.

10. So far as the first question is concerned, the fact that the Tribunal rendered its decision without taking note of the aforesaid explanation to Rule (1) in Schedule II was undoubtedly a ground for rectification. The Tribunal's power to rectify its orders under the Act flows from Section 13 of the Act. Mistake apparent from the record is made a ground for rectifying the order. The first question was, thus, rightly answered in favour of the Revenue and against the Assessee.

11. The second question contains four items and the question is whether they are merely provisions or reserves. For a proper appreciation of the first item of Rs. 4,50,000/-, being the amount set apart for contingent liabilities, it is necessary to state a few facts. On 18.8.1956, the Assessee had applied to the Commissioner of Income Tax requesting him not to invoke the provisions of Section 23 A of the Indian Income Tax Act, 1922 against it. Pending the said application it had set apart a sum of Rs. 6,52,000/- for meeting the liability in the accounting year ending on 31.3.1956. During the financial year 1958-59, a sum of Rs. 2,02,000/- was transferred from this amount to the general reserves through profit and loss account, with the result that a sum of Rs. 4,50,000/- continued to be shown in the balance-sheet as provision for taxation as on 1st April, 1963. By his order dated 15.4.1957, the Commissioner

rejected the assessee's application dated 18.8.1956 against which the assessee filed an appeal before the Board of Referees. This appeal too was rejected against which the assessee moved the High Court of East Punjab by an application dated 21.6.1958. It too was rejected on 18.1.1962 against which a Letters Patent Appeal was preferred. Meanwhile, the Income Tax Officer passed an order under Section 23A of 23.7.1963 levying additional tax. (Subsequently, however, the Letters Patent appeal preferred by the assessee was allowed on 24.5.1965 with the result that the order of the Income Tax Officer stood vacated but that is a subsequent circumstance which we cannot take note of in proceedings for the year relating to assessment year 1964-65). From the above statement of facts, it is clear that the amount of Rs. 4,50,000/- was a provision made to meet a tax liability existing on the relevant late. By no stretch of imagination can it be treated as a reserve. Similarly, the second item, an amount of Rs. 15,82,000/- set apart for proposed's dividend cannot also be treated as a reserve but as a provision for meeting a current liability. The same must be said about the third item of Rs. 6,99,913/-, the amount set apart for profit sharing bonus. With respect to the last item of Rs. 50,000/- which was a provision for pension scheme, there can equally be no dispute that it is a provision.

12. In view of our answers to questions 1 and 2, the third question need not be answered. Coming to the fourth question which has been referred at the instance of the Revenue, it may be noticed that the amount of Rs. 9,97,410/- credited to the Depreciation Fund was the excess amount over the amount actually allowed as depreciation in the assessments made under the Income Tax Act. It thus clearly constitutes reserves as per the decision in Vazir Sultan. The High Court was right in answering the same in favour of the Assessee and against the Revenue.

13. For the above reasons, both the appeals fail and are dismissed. No costs.