

R.B. Seth Multanimal And Sons vs Commissioner Of Income-Tax, U.P. And ... on 27 August, 1952

Equivalent citations: AIR1953ALL31, [1952]22COMPCAS264(ALL), [1952]22ITR331(ALL), AIR 1953 ALLAHABAD 31

Author: V. Bhargava

Bench: V. Bhargava

JUDGMENT

Malik, C.J.

1. This is a reference under Section 21, Excess Profits Tax Act read with Section 66(1), Income-tax Act. The question referred to this Court is as follows :

"Whether in the circumstances of the case, the remuneration granted to R.B. Seth G.M. Modi is directors' remuneration within the meaning of the term as used in Schedule 1, Rule 7 (1), Excess Profits Tax Act read with Clause (2) (a) of the same rule?"

There was a Hindu undivided family firm known as R.B. Multanimul and Sons which till March 1940 worked as Managing Agents of the Modi Sugar Works Ltd. There was a disruption in the family and the Hindu undivided family firm was succeeded by another firm of the same name which carried on business up to September 1940. In September 1940, a private limited company was formed which took over as a going concern the business of R.B. Multanimul and Sons and thus became the Managing Agents of the Modi Sugar Works Ltd. From the Articles of Association of the Company it appears that the Board of Directors could not exceed 7 including the Governing Director and could not be less than 2.

The names of the first set of 5 Directors were given in the Articles of Association and they were R.B. Seth Multanimul, Raizada Seth G. M. Modi, Seth Harmukhrai, Seth Harnam Singh and Seth Benarsidas. Raizada Seth G. M. Modi was under Article 61 appointed Governing Director subject to the control and supervision of the Board of Directors. His functions were defined in Article 62, Article 61 provides that he was to be the Governing Director for his lifetime and he was also given the right to nominate, assign or appoint a successor or appoint his administrator or executor to be the Governing Director of the Company in his place. As Governing Director of the company he was paid certain remuneration and the Appellate Tribunal held that the amount paid to Raizada G. M. Modi was paid to him as Director of the company and the amount was, therefore, not a deductible

expenditure from the total profits calculated for purposes of payment of the Excess Profits Tax.

2. 'Director' is defined under Section 2 (10), Excess Profits Tax Act as including any person occupying the position of a director by whatever name called and also includes any person who is a manager of the company or is concerned in the management of the business, is remunerated out of the funds of the business and is the beneficial owner of not less than 20 per cent, of the ordinary share capital of the company. Seth G. M. Modi owns only 10 per cent, shares in the company and not 20 per cent. It was, therefore, urged that Seth G. M. Modi was performing two separate functions, one of a director and the other of a manager, and as manager, by reason of the fact that he was not the beneficial owner of 20 per cent, of ordinary share capital of the company, he could not be called a director.

3. On behalf of the Department it was urged that it was not their case that Seth G. M. Modi was manager of the company and as he held beneficial ownership in not less than 20 per cent, ordinary share capital of the company he was deemed to be a director, but that the whole amount paid to him was paid to him as a director and that the case came under Schedule 1, Rule 7 (2), Excess Profits Tax Act.

4. 'Profits' are defined in Section 2, Sub-section (19) as meaning profits as determined in accordance with Schedule 1 ; and Rule 7 (1) Schedule 1, provides that in computing the profits or standard profits no deduction can be made in respect of director's remuneration. Sub-rule (2) of Rule 7 of the same Schedule provides that :

"The expression "director's remuneration" does not include :

(a) the remuneration of any director who is required to devote substantially the whole of his time to the service of the company in a managerial or technical capacity and is not the beneficial owner of, or able, either directly or through the medium of other companies or by any other indirect means, to control, more than five per cent. of the ordinary share capital of the company, or

(b) the remuneration of any managing agent where such remuneration is included in the profits of the managing agent's business for the purposes of excess profits tax."

The question, therefore, is whether the remuneration, which the company wanted to deduct and the Appellate Tribunal has held that it was not entitled to deduct, was paid to Seth G. M. Modi as director, who was required to devote substantially the whole of his time to the service of the company, it being admitted that he owned more than 5 per cent. ordinary shares, or it was paid to him as manager.

5. Learned counsel for the assessee has urged that Seth G. M. Modi was performing dual functions of a director and a manager and the remuneration paid to him as manager cannot be said to be paid to him as director for performing any managerial work entrusted to the director. The whole basis of the argument is that under Article 61 of the Articles of association Seth G. M. Modi had to carry on the

work assigned to him subject to the control and supervision of the Board of Directors and it is urged that Seth G. M. Modi, therefore, became a manager of the company. Reliance is placed on the definition of the word 'manager', in the Indian Companies Act. The word 'manager' has been defined in Section 2(9) of that Act "as a person who, subject to the control and direction of the directors, has the management of the whole affairs of a company". The argument is that, if he was to carry on the work assigned to him as a director and not as a manager, then he should not be subject to the control and supervision of the other directors and since he was to work subject to the control and supervision of other directors he must be deemed to be performing the functions of a manager in addition to his duties as director and ceased to be a director simpliciter.

Learned counsel has urged that the word 'manager' is not defined in the English Statute and, therefore, English cases are not likely to be of much assistance. Reference, however, was made to the case *Henry Richardson, Ltd. v. Inland Revenue Commissioners*, (1947) 1 ALL E. R. 275. In that case C was the secretary of the company and later became a director. As secretary she was drawing a salary and as director she became entitled to receive the fees payable to other directors together with certain bonuses. The question for decision was whether the whole amount paid to her as salary as secretary as well as the fees and bonuses paid to her as director became remuneration paid to her as a director. On behalf of the Inland Revenue Commissioners, it was urged that having become a director of the company whatever amount she received must be deemed to be director's remuneration. It was pointed out, on the other hand, that having continued to be the secretary it might well be urged that all that she received was secretary's remuneration.

The learned Judge (Atkinson J.), however, pointed out that the question had to be decided on a consideration of the fact whether she continued to hold two offices, her duties as secretary being separate from her duties as Director and Chairman of the Board, and that whether if she ceased to be a Director, the post of Secretary would remain and her salary as Secretary would remain payable to her. The learned Judge further pointed out that Directors are of two kinds: Directors who merely attend Directors' meetings and get Directors' fees; and working Directors who give all their time to carrying on the business of the company, such as a Managing Director, and in the latter case the amount paid to the Managing Director would be remuneration paid to a Director.

6. In the case before us it cannot be seriously urged, that Seth G. M. Modi held two distinct and separate offices, one of director and the other of manager. The definition of a manager in the Companies Act is very wide and "includes a director or any other person occupying the position of a manager by whatever name called and whether under a contract of service or not".

The Indian Companies Act thus contemplates managers who might be servants of the company under contract of service as also managers who might not be servants but might be carrying on the work of a manager in some other capacity such as the capacity of a director. It is only if a person is a manager under a contract of service that the remuneration paid to him can be said to be the remuneration paid to a manager simpliciter. In case where the person happens to be in charge of some managerial work because of some other capacity occupied by him the remuneration paid to him need not necessarily be held to be remuneration paid to him in his capacity as manager.

We may take the example of a managing agent. The managing agent is also under the control and direction of the directors "except to the extent if any, otherwise provided for in the agreement" and is entitled to the management of the whole affairs of the company by virtue of an agreement with the company. If by virtue of this right a managing agent actually has the management of the whole affairs of the company, he may be doing the same work as a manager is expected to do under the Indian Companies Act, still the remuneration paid to him must be held to be managing agent's remuneration. Similarly, if a director has the management of the affairs of a company entrusted to him in his capacity as a director, the remuneration paid to him will be director's remuneration even though the work entrusted to him might be the same as is usually done by a manager. It will cease to be director's remuneration only if he happens to be doing the work not in his capacity as a director to whom some additional work has been entrusted but as a manager in the capacity of a servant under a contract of service so that he is really holding two distinct and separate offices.

In *Hutton v. West Cork Railway Co.*, (1883) 23 Ch. D. 654, it was pointed out by Bowen L. J. that a director is not a servant of the company and whatever amount is paid to him is paid as gratuity. In the case before us there can be no doubt that Seth G. M. Modi was entrusted, under Article 62 of the Articles of Association, with certain functions by virtue of his having been appointed Governing Director and it was never the intention under that Article to appoint him as a manager under a contract of service with the company. He did not occupy two distinct and separate offices, one of manager and the other of director. He, as Governing Director, was entitled to continue in that office for the rest of his life and his rights were to go to his successor, administrator or executor after his death. He was further given the right to assign his rights or nominate his successor. He was to be the Chairman of the Board and was to preside at all meetings of the Board. Under Article 68 of the Articles of Association, though all other directors had to vacate office on being requested in writing to do so by the co-directors, the Governing Director could not be so removed. In Article 62 of the Articles of Association the various functions to be performed by the Governing Director, without prejudice to the general powers conferred on him by Article 61, are enumerated which include the power to appoint a manager. If he chose to appoint a manager in exercise of his power as the Governing Directors, he would cease to be the manager of the company as defined under the Indian Companies Act and yet he would be entitled to the remuneration fixed for him under Article 61 of the Articles of Association.

It cannot be seriously contended that Seth G. M. Modi could have continued to exercise the functions entrusted to him under Article 62 as Governing Director, if he had ceased to be director of the company. It is clear that the remuneration payable to him under Article 61 was payable in his capacity as a Governing Director irrespective of the fact whether he also discharged the functions of the manager under the Indian Companies Act or entrusted such functions to any other person appointed by him.

7. We are, consequently, satisfied that, on the facts and circumstances of this case, the remuneration granted to R.B. Seth G. M. Modi was director's remuneration within the meaning of the term as used in Schedule I, Rule 7 (1), Excess Profits Tax Act read with Clause 2 (a) of the same rule.

8. The assessee must pay the costs of the other side which we assess at Rs. 500.