Anglo-French Textile Co. Ltd vs Commissioner Of Income-Tax, Madras on 22 December, 1952

Equivalent citations: 1953 AIR 105, 1953 SCR 454

Author: Mehr Chand Mahajan

Bench: Mehr Chand Mahajan, Vivian Bose, Natwarlal H. Bhagwati

PETITIONER:
ANGLO-FRENCH TEXTILE CO. LTD.

Vs.

RESPONDENT:
COMMISSIONER OF INCOME-TAX, MADRAS,

DATE OF JUDGMENT:
22/12/1952

BENCH:
MAHAJAN, MEHR CHAND
BENCH:
MAHAJAN, MEHR CHAND
DAS, SUDHI RANJAN
BOSE, VIVIAN
BHAGWATI, NATWARLAL H.

CITATION:
1953 AIR 105 1953 SCR 454
CITATOR INFO :
C 1954 SC 198 (10,10A)
R 1958 SC 269 (14)
R 1958 SC 861 (15)
RF 1965 SC1526 (15)

ACT:
Income-tax Act, 1922, ss. 4 (1) (a), 4A (c) (b), 42 (1) and (3) -Foreign company-Manufacture of goods outside British India -Sale of goods and receipt of sale proceeds in British India Assessment under s. 4 (1) (a)-Applicability of s. 42 (1)Determination of residence of company-Allocation of income between operations carried on within and outside British India Whether permissible.

HEADNOTE:
The assessee, a company incorporated in the United Kingdom

and having its registered office in London, manufactured yarn and cloth in their,mill at Pondicherry. The assessee had appointed another company in Madras as their agents. The manufactured goods were sold mostly in British India and partly outside British India. All the contracts in respect of the sales in British India: were entered into in British India and deliveries were made and payments were received in British India. In regard to sales outside British India also, payments were received in Madras

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through the agents and it was found as a fact that, the entire profits were received in India:

Held, (i) that in view of the finding of fact that the entire profits were received in India and the assessee was liable to tax under s. 4 (1) (a), the provisions of s. 42 (1) had no relevancy ;

(ii)that the income received in British India could not be said to wholly arise in British India within the meaning of s. 4A (c) (b) and that there should be allocation of the income between the various business operations of the assessee demarcating the income arising in the taxable territories in the particular year from the income arising without the taxable territories in that year for the purposes of s. 4A (c) (b) of the Act.

Commissioner of Income-tax, Bombay v. Ahmedbhai Umarbhai & Co. ([1950] S.C.R. 335), Pondicherry Railway Company v. Commissioner of Income-tax, Madras [1931] (58 I.A. 239), Turner Morrison and Co. v. Commissioner of Income-tax [1951] (19 I.T.R. 451 ; [1953] 23 I.T.R. 152), referred to.

JUDGMENT:

CIVIL APPELLATE JURISDICTION: Appeal No. 1 1 of 1952. Appeal from the Judgment and Order dated January 18, 1950, of the High Court of Judicature at Madras (Satyanarayana Rao and Viswanatha Sastri JJ.) in Case Referred No. 25 of 1947. O.T.G. Nambiar (Samarendra Nath Mukherjee, with him I for the appellant.

M. C. Setalvad, Attorney-General for India, and C. K Daphtary, Solicitor-General for India (G. N. Joshi and P.A. Mehta, with them) for the respondent.

1952. December 22. The Judgment of the Court was delivered by BHAGWATI J.-This is an appeal from the judgment and order of the High Court of Judicature at Madras upon a reference made by the Income-tax Appellate Tribunal under section 66(1) of the Indian Incometax Act, 1922. The appellant company, the assessee, is incorporated in the United Kingdom under the English Companies Act and has it registered office in London. It owns a spinning and weaving mill at Pondicherry in French India where it manufactures yarn and cloth. Messrs. Best and Co. Ltd., Madras, have been appointed the agents of the assessee under an agreement dated, the 11th July,

1939, and have been invested with full powers in connection with the business of the assessee in the matter of purchasing stock, signing bills and other negotiable instruments and receipts and settling, compounding or compromising any claim by or against the assessee. The yarn and cotton manufactured in Pondicherry were sold mostly in British India and partly outside British India. In the accounting year 1941 and 1942 all the contracts in respect of the sales in British India were entered into in British India and the deliveries were made and payments received in British India. In regard to the sales outside British India also, payments in respect of such sales were received in Madras through the said agents.

The total sales of the goods in the assessment year 1942-43 were Rs. 69,69,145 and for the assessment year 1943-44 were Rs. 93,48,822. The value of the sales in British India amounted to Rs. 57,07,431 for the assessment year 1942-43 and to Rs. 67,98,356 for the assessment year 1943-44. The value of the total sales outside British India amounted to Rs. 12,61,714 for the year 1942-43 and Rs. 25,50,472 for the year 1943-44. Out of the said amounts received in respect of the foreign sales the amounts received in British India were Rs. 9,62,434 for 1942-43 and Rs. 75,230 for 1943-44 and the amounts received outside British India were Rs. 2,99,280 for 1942-43 and Rs. 24,75,242 for 1943-44.

On these facts the Income-tax Officer found that the assessee was resident in British India within the meaning of section 4-A (c) (b) of the Act by reason of its income arising in British India in the year of account exceeding its income arising without British India and on that basis he assessed the company for the two assessment years 1942-43 and 1943-44 as - resident in British India on the profits and gains which had accrued to the company both within and without British India under section 4 (1) (b) (i) and (ii) of the Act. The order of the Income-tax Officer was confirmed by the Appellate Assistant Commissioner and, the order of the Appellate Assistant Commissioner was confirmed by the Appellate Tribunal on the 15th May, 1946.

The assessee applied to the Appellate Tribunal under section 66 (1) of the Act for reference to the High Court of certain questions of law arising out of its order. The, Commissioner of Income-tax in his reply suggested the following two questions for reference (1)Whether on the facts and in the circumstances of the case, the Appellate Tribunal was right in holding that section 42 (1) and (3) of the Income-tax Act has no application to income accruing or arising to the assessee company in British India or to income received by it in British India during the previous year?"

> " (2) Whether, on the facts and in the circumstances of the case, the Appellate Tribunal was right in holding that the entire income of the assessee company during the accounting year ended 31st December, 1941, was assessable under section 4(1) of the Incometax Act, and that no portion of such - in come was entitled to be exempted under section 42(3) of the Act ?

The Appellate Tribunal however referred the following questions to the High Court:-

> " (1) Whether on the facts and in the circumstances of the case, section 42 (1) and (3) of the Act alone and not section 4 of the Act have application to the income accruing

> or arising to the assessee company in British India and to the income attributable to the sale proceeds received by it in British India during the previous year?"
>
> " (2) Whether on the facts and in the circumstances of this case the entire profits and gains arising to the assessee company in British India should be taken into account for the purpose of applying the test laid down under section 4-A
>
> (c) (b) or only that part of the profits which should be determined after the application of sectioin 42(3) of the Act as reasonably be attributable to that part of the operations carried on in British India ?" and " (3) Whether on the facts and in the circumstances' of the case, the provisions. of the Indian Income-tax Act contained in section 4 (1) with the subsections and section 4-A (c) (b) are not ultra vires in so far as they seek to assess foreign income of the company registered outside British India ?"

The third question was concluded by the decision of their Lordships of the Privy Council in the case of Wallace Bros. & Co. Ltd. (1) and was therefore not argued before the High Court and the High Court answered it by stating that the provisions of section 4 (1) and section 4-A (c) (b) of the Act were not ultra vires the Indian Legislature. The question No. (1) was further amended by agreement between the learned counsel for the revenue authority and the assessee and it was reframed as under:

> " (1) Whether on the facts and in the circumstances of the case section 42 (1) and (3) of the Act alone and not section 4 of the Act have application to the income accruing or arising by reason of sales in British India of manufactured goods where the manufacturing process took place outside British India?"

The question (2) was retained in the form in which it had been referred by the Appellate Tribunal. Both these questions were answered against the assessee by the High Court. The assessee obtained the necessary certificate from the High Court for leave to appeal to this court and hence this appeal.

It may be observed that in reply to the. notice under sections 22(2) and 38 of the Act for the assessment year 1942-43 the agents of the assessee had on the 1st June, 1943, submitted a return under protest and had claimed that the income shown in the return should be apportioned under section 42(3) of the Act as between the operations carried on in British India and operations carried on outside British India. They had further declared that the company was non-resident in British India during the previous year for which the return was made. In the statement enclosed

-therewith the total world income for the year ended 31st December, 1941, had been shown at Rs. 10,23,907. Profit at 10 per cent. on British Indian sales which (1) (1948) 76 I.A. 86.

aggregated to Rs. 57,07,431 was shown at Rs. 5,70,743 and after deduction of the proportionate expenses relating to sales in British India and sundry charges was put down at the net figure of Rs. 4,58,026 which was shown as the British Indian income. It was thus contended that the income

arising in British India in the year of account did not exceed its income arising without British India and that therefore the assessee was non-resident in British India. This calculation of profits at the rate of 10 per cent. on British Indian sales did not make any allocation between manufacturing profits and merchanting profits and all the profits arising out of British Indian sales were shown in one lump sum. The Income-tax Officer took it as settled law that the profits arose in the country in which the sales took place and as the bulk of the sales had taken place in British India the bulk of the profits accrued or arose in British India. He held that the provisions of section 42(3) would apply only where the profits arose outside British India but which by virtue of section 42(1) were deemed to accrue or arise in British India, and that it did not apply where the profits actually arose in British India by the sale of goods in British- India. He therefore held that the entire profits on "Sales made in British India actually arose in British India and were liable to tax under section 4 (1) (c). On a calculation of the figures he came to the conclusion that the income of the assessee arising in British India in the accounting year exceeded its income arising without British India and that the assessee was resident in British India under section 4-A(c). The assessee was also held ordinarily resident in British India under section 4-B(c) and he assessed the company accordingly on that basis. The Appellate Assistant Commissioner also proceeded on that basis and confirmed the order of the Income-tax Officer. He was however further of the opinion that the entire profits were received where the sale pro- ceeds were received and the assessee was therefore. liable to tax under section 4(1)(a) also. This conclusion was arrived at by him relying upon two decisions of their Lordships of the Privy Council: (1) Pondicherry Railway Company V. Commissioner of Income-tax, Madras(1) and Commissioner of Income-tax, Madras v. Diwan Bahadur Mathias(2), in the first of which at page 369 Lord Macmillan observed as follows : Their Lordships accordingly are of the opinion that the income derived by the Pondicherry Railway Company from the payment made to them by the South Indian Railway Company is on the facts stated received in British India within the meaning of the Act by the Agent of the Pondicherry Railway Company there on their behalf " It is unnecessary to go on to consider whether the business is carried on in British India, which is the form which question (c) takes, for it is enough if the profits of a business carried on by the assessee are received in British India and the place where the business is carried on is not material." The Appellate Tribunal adverted to the fact that the whole income of the company, so far as 1942-43 is concerned was received in British India and so far as 1943-44 is concerned a major part of it in this way was received in British India, but did not base its decision on this aspect of the case. It held that the scope of section 42(3) was circumscribed by confinement to those cases where profits were deemed to accrue or arise under section 42 alone and there was no warrant for extending the principle of apportionment to other cases where the profits and gains were made taxable under other sections of the Act. It also held that section 42 dealt with " deemed " income whereas section 4-A (c) dealt with income that arose in British India. Therefore, it could not be said that for the purpose of section 4-A (c) a proportionate "deemed " income should be taken as income that arose in British India. When the application for reference was made to the Appellate Tribunal the Commissioner of Income-tax in the question (1) which he suggested included within its ambit this aspect of the income having been received by the assessee in British India during the previous year. But when the Appellate Tribunal refrained the question (1) it merely (1) (1931) 5 I.T.C. 363- (2) [1939] 7 I.T.R- 48.

confined it to income accruing and arising to the assessee in British India and to the income attributable to the sale proceeds received by it in British India during the previous year. The

question (1) as finally framed by the High Court adverted to the income accruing or arising by reason of sales in British India on manufactured goods where manufacturing process took place outside British India and the aspect of the income having been received by the assessee in British India was absolutely ignored. When the questions were originally referred to the High Court the position in law as then understood was that profits arose in the country in which the sales took place. This position was however negatived, particularly in the case of manufacturing businesses, in a decision of this court. in Commissioner of Income-tax, Bombay v. Ahmedbhai Umarbhai & Co., Bombay(1).

After hearing at considerable length the arguments urged before us on behalf of the assessee as well as the Income- tax authorities we feel that in view of that decision the questions framed by the Tribunal and the High Court do not bring out the real point in controversy between the parties and it is agreed that the following two questions truly represent I and bring out the matter on which the parties are at issue. We therefore resettle the questions originally framed and reframe them as below:

> (1) Whether in view of the finding of fact in this case that the entire profits were received in India and the company is liable to tax under section 4 (1) (a) of the Act, the provisions of section 42(1) have any relevancy ? (2) Can the income received in India be said to arise in India within the meaning of section 4-A(c)(b) of the Act ?

If not, should only those profits determined under section 42(3) as attributable to the operations carried out in India be taken into account for applying the test laid down in section 4-A (c) (b) ?

(1) [1950] S.C.R. 335; 18 I.T.R. 472.

The case is remanded to the High Court with the direction that it should give its opinion on, these two questions and submit the case to this court within three months. S. N. Mukherjee, for the appellant.

Porus A. Mehta, for the respondent.

1953. December 8. BHAGWATI J.-By our judgment dated the 22nd December, 1952, we reframed the questions as below:

> (1) Whether in view of the finding of fact, in this case that the entire profits were received in India and the company is liable to tax under section 4 (1) (a) of the Act, the provisions of section 42 (1) have any relevancy; (2) Can the income received in India be said to arise in India within the meaning of section 4A (c) (b) of the Act ?

If not, should only those profits determined under section 42 (3) as attributable to the operations carried out in India be taken into account for applying the test laid down in section 4A (c) (b), and remanded the case to the High Court with the direction that it should give its opinion on these two questions. The High Court has accordingly considered these two questions which were referred to it

for opinion and has answered the question No. I in the negative and against the assessee and question No. 2 in the manner following, i.e., the income received in British India cannot be said to wholly arise in India within the meaning of section 4A (c) (b) of the Act and that there should be allocation of the income between the various profit producing operations of the business of the company in the light of the principle contained in the judgments in Ahmedbhai Umarbhai's case(1) and in Anglo- French Textile Company v. Income-tax Commissioner(2) relating to the same assessee.

When the matter came up for further arguments before us on this opinion of the High Court,Shri S. N. Mukherjee, the learned counsel for the appellant (1) (1950] 18 I.T.R. 472, (2) A.I.R, 1953 SCR 105 did not contest the correctness of the answer to question No. I in view of the decision of this court in Turner Morrison & Co., Ltd. v. Commissioner of Incometax, West Bengal(1). It may be noted that even before the High Court the learned counsel appearing for both the parties agreed that the matter was concluded by this decision against the assessee and question No. I was answered accordingly by the High Court.

In regard to the question No. 2 however Shri Porus A. Mehta, learned counsel for the respondent, contended before us that the matter was not concluded by the judgment of the majority in Commissioner of Income-tax, Bombay v. Ahmedbhai Umarbhai & Co., Bombay(1) and that the High Court was wrong in the answer which it gave to this question. He contended that the decision in the case of Commissioner of Income-tax, Bombay v. Ahmedbhai Umarbhai & Co., Bombay("), turned on the statutory provisions of the Excess Profits Tax Act read with section 42 (3) of the Indian Income-tax Act which was expressly incorporated therein by virtue of section 21 of the Act and not on any general principles of apportion. ment of income, profits or gains enunciated therein. He took us in extensover the portions of the majority judgments and tried to demonstrate that the decision there was based purely on the applicability of section 42 (3) of the Indian Income-tax Act, but for the applicability of which, according to his submission, there was no room for the apportionment of the income, profits or gains of the business, in the manner contended by the appellant. We do not accept this contention of the respondent. Section 4A(c)

(b) is concerned with the income arising in the taxable territories in a particular year exceeding the income arising without the taxable territories in that year and the very words of the section are capable of being construed as also contemplating a state of affairs where there may have to be a division or apportionment between the income arising in the taxable territories and the income arising without the taxable territories (1) [1953] S.C.R. 520.

(2) [1950] S.C.R 335.

in the particular year. The whole of the argument urged before us on behalf of the respondent was aimed at establishing that the scheme of the Indian Income-tax Act was not to tax the source of income but the income, profits or gains from whatever source derived which were received or were deemed to be received in the taxable territories or which accrued or arose or were deemed to accrue or arise in the taxable territories during the particular year and that it was immaterial whether the income, profits or gains were derived from business operations carried on in the taxable territories

or without the taxable territories. This argument was possible when the decisions which held that income, profits or gains arose or accrued at the places where the sales took place were good law, because then there was no question of apportionment of income, profits or gains arising from the business operations carried on in the taxable territories 'and income, profits or gains arising from the business operations carried on without the taxable territories. The moment however it was held, as it was done in Commissioner of Income-tax, Bombay v. Ahmedbhai Umarbhai & Co., Bombay(1), that though profits may not be realised until a manufactured article was sold profits were not wholly made by the act of sale and did not necessarily accrue at the place of sale and to the extent profits were attributable to the manufacturing operations profits accrued at the place where business operations were carried on, these decisions went by the board. The question whether a particular part of the income, profits or gains arose or accrued within the taxable territories or without the taxable territories would have to be decided having regard to the general principles as to where the income, profits or gains could be said to arise or accrue. Section 42 of the Indian Income-tax Act has no relevance to the determination of this question because it is mainly concerned with income Which is deemed to have arisen, or accrued and not with income which actually arises or. accrues within the taxable Territories. Section 42 (3) also is a part of the' scheme which is enacted in section 42 and cannot help (1) (1950)S.C.R. 335.

in the determination of the question before us As a matter of fact the use of the words "under section 42(3)" used in the question No. 2 as reframed by us was not appropriate and the only question which should have been sent to the High Court was "If not, should only those profits determined as attributable to the operations carried out in India be taken into account for applying the test laid down in section 4A

(c) (b)."

If, therefore, section 42(3) has nothing to do with the determination of the income arising in the taxable territories as distinguished from the income arising without the taxable territories as understood in section 4A(c) (b) of the Act what we have got to consider is whether there is anything in the Act which prevents the application of the general principle of apportionment of income, profits or gains between those which are derived from business operations carried on within the taxable territories and those which are derived from business operations carried on without the taxable territories. The contention which was advanced by Shri Porus A. Mehta on behalf of the respondents in this behalf, viz., that the word ,arise " was the only word used in section 4A (c) (b) and the word "accrue" did not find any place therein, that there was a distinction between the conception of arising and the conception of accrual and that the apportionment of the income was appropriate only in cases where the income arose and was inappropriate in cases where the income accrued, was sufficiently repelled in the judgment in Commissioner of Income-tax, Bombay v. Ahmedbhai Umarbhai &.Co., Bombay(1), where it was observed:

> " Whether the words 'derive' and 'Produce' are or are not synonymous with the words'accrue' or arise it can be said without hesitation that the words 'accrue' or " arise' though not defined in the Act are certainly synonymous and are used in the sense of 'bridging, in as a natural result'. Strictly speaking, the word 'accrue' is not

synonymous with 'arise', the former connoting idea of growth or accumulation and the (1) [1950] S.C.R. 335 at p. 364.

latter of the growth or accumulation with a tangible shape so as to be receivable. There is a distinction in the dictionary meaning of these words, but throughout the Act they seem to denote the same idea or ideas very similar and the difference only lies in this that one is more appropriate when applied to a particular case. In the case of a composite business, i.e., in the case of a person who is carrying on a number of businesses, it is always difficult to decide as to the place of the accrual of profits and their apportionment inter se. For instance, where a person carries on manufacture, sale, export and import, it is not possible to say that the place where the profits accrue to him is the place of sale. The profits received relate firstly to his business as a manufacturer, secondly to his trading operations, and thirdly to his business of import and export. Profit or loss has to be apportioned between these businesses in a businesslike manner and according to well-established principles of accountancy. In such cases it will be doing no violence to the meaning of the words accrue' or 'arise' if the profits attributable to the manufacturing business are said to arise or accrue at the place where the manufacture is being done and the profits which arise by reason of the sale are said to arise at the place where the sales are made and the profits in respect of the import and export business are said to arise at the place where the business is conducted. This apportionment of profits between a number of businesses which are carried on by the same person at different places determines a so the place of the accrual of profits." The phraseology of section 42(3) of the Act'also repels the contention in so far as the profits and gains of the business which are referred to therein and which are capable of apportionment as therein mentioned are deemed to accrue or arise in the taxable territories thus using the words "accrue" and "arise" as synonymous with each other. The above passage is also sufficient in our opinion to establish that the apportionment of income, or gains between those arising from business opinion carried on in the taxable territories and those arising from business operations carried on without the taxable territories is based not on the applicability of section 42(3) of the Act but on general principles of apportionment of income, profits or gains. That was really the ratio of the judgment of the majority in Commissioner of Income-tax, Bombay v. Ahmedbhai Umarbhai & Co., Bombay(1), and any attempt to distinguish that 'ease from the present one by having resort to the statutory provisions of the Excess Profits Tax Act is really futile. We are accordingly of the opinion that the answer given by the High Court to the question No. 2 also was correct.

The appeal before us will accordingly be allowed and the answers to the questions Nos. 1 and 2 refrained by us will be as under:-

> Question No. 1-In the negative; and Question No. 2-The income received in British India cannot be said to wholly arise in India within the meaning of section 4A (c) (b) of the Act and that there should be allocation of the income between the various business operations of the assessee company demarcating the income arising in the taxable territories in the particular year from the income arising without the taxable territories in that year for the purposes of section 4A (c) (b) of the Act. In so far as the appellant has failed in one part of the case and succeeded in another part we think that the proper order for cost should be that each party bears and pays his own costs

of this appeal including ,the costs of the remand before the High Court.

Appeal allowed.

Agent for the appellant: P. K.. Mukherjee. Agent for the respondent: G. H. Rajadhyaksha.