Netherlands Steam Navigation Company ... vs The Commissioner Of Income-Tax, West ... on 14 March, 1969

Equivalent citations: 1969 AIR 1262, 1970 SCR (1) 1, AIR 1969 SUPREME COURT 1262

Author: J.C. Shah

Bench: J.C. Shah, V. Ramaswami

PETITIONER:
NETHERLANDS STEAM NAVIGATION COMPANY LTD.

Vs.

RESPONDENT:
THE COMMISSIONER OF INCOME-TAX, WEST BENGAL

DATE OF JUDGMENT:
14/03/1969

BENCH:
SHAH, J.C.
BENCH:
SHAH, J.C.
RAMASWAMI, V.

CITATION:
1969 AIR 1262 1970 SCR (1) 1
1969 SCC (2) 84

ACT:
Income-tax Act 1922 section 10(2) (vi-a)-Non-resident-Company -Taxable profits computed by special formula evolved by Income-tax Officer and not under second method in rule 33 Income-tax Rules of 1922-Whether initial and additional depreciation admissible.

HEADNOTE:
The appellant is a non-resident shipping company with its local office in Calcutta. For its assessment to income-tax for the years 1952-53 to 1956-57 the appellant filed returns disclosing taxable income computed on the basis of its annual turn-over in its Indian trade but did not furnish particulars of its world income. The Income-tax Officer computed the taxable business income for each year by

application of a special formula which was accepted by the appellant. However, in computing the income, the Income-tax Officer only allowed normal depreciation and other trade allowances admissible under the income-tax Act 1922 and did not allow any initial depreciation or additional depreciation in respect of the ships of the appellant in any of the assessment years, because the ships acquired by the appellant were not introduced into the Indian business in the years in which they were newly acquired. The, orders of assessment were confirmed by the Appellate Assistant Commissioner but the Tribunal held that in respect of all the four ships, additional depreciation wag 'admissible under section 10(2) (vi-a) of the Act, as claimed. The High Court, on a reference, answered the question against the assessee.

HELD : Additional depreciation was not admissible to the appellant as an allowance in the computation of the taxable income by the special formula adopted by the Income-tax Officer.

It was common ground that the, appropriate method for determining the profits was the second method in r. 33. But that method was never applied; if it was applied in the computation of the world profits of the assessee, it would have been necessary to allow the various depreciation allowances. The assessee could not, while accepting determination of taxable profits in a manner not warranted by the second method under r. 33, claim that additional depreciation should be allowed. [8 E]

The Supreme Court in the present appeal was exercising an advisory jurisdiction and could not decide whether the computation of taxable income by the Incometax Officer by the application of the formula evolved by him was correct. Additional depreciation is a statutory allowance in the determination of taxable profit under s. 10 of the Act, and in the case of a non-resident where, actual income cannot be determined, and resort is had to r. 33, not when an empirical method is adopted for computation of the taxable income. [7 H]

JUDGMENT:

CIVIL APPELLATE JURISDICTION: Civil Appeals Nos. 1622 to 1626 of 1968.

Appeals from the judgment and order dated February 11, 1964 of the Calcutta High Court in Income-tax Reference No. 109 of 1960.

Sachin Chaudhuri, T. A. Ramachandran and D. N. Gupta, for the appellant (in all the appeals).

S. T. Desai, S. A. L. Narayan Rao, R. H. Dhebar, R. N. Sachthey and B. D. Sharma, for the respondent (in all the appeals).

The Judgment of the Court was delivered by Shah, J. Netherlands Steam Navigation Company Ltd.-hereinafter called "the assessee"-is a non-resident Company engaged in shipping business. For the assessment years 1952-53 to 1956-57 the assessee filed its return of income for the relevant accounting years disclosing taxable income computed on the basis of its annual turnover in its Indian trade i.e. "round voyages" to and from Indian Ports. The assessee did not furnish particulars of its world income. The Income-tax Officer computed the taxable business income of the assessee for each year by the application of the following formula:

Indian trade profits x Indian Port receipts

Total Port receipts By the expression "Indian trade profits" in the formula was meant profit earned in "round voyages" made by the assessee's ships which touched Indian ports. Operation of the formula may be illustrated by taking a sample computation by the Income-tax Officer for the year 1953-54 -

Kr. Kr.

"Total gross earning in Indian Trade 10,024,996 Deduct:--

(1)	Total experience in Indian Trade	7,705,474	
(2)	Depreciation allowance	733,671	8,439,145
	Net profit India Trade		1,585,851
	Gross earning from Indian Ports		5,440,042
	Proportionate Indian Profits:---		
	5,440,042 ----------* 1,585,851		860,559
	100,024,996		
	(Rs.100=Kr.79.80		Rs.10,78,395"

In computing the profits of the assessee in India in each year the Income-tax Officer allowed normal depreciation and other trade allowances admissible under the Indian Income-

tax Act, 1922, and the relevant rules made thereunder. He, however, did not allow initial depreciation and additional depreciation in respect of the ships of the assessee in any of the assessment years, because the ships acquired by the assessee were not introduced into the Indian business in the years in which they were newly acquired. 'The orders of 'assessment were confirmed by the Appellate Assistant Commissioner.

In appeal to the Income-tax Appellate Tribunal the assessee claimed Additional depreciation for four ships for which the following details were furnished:

> "(1) S. S. Bintang Brought into use in 1950.Brought into use in the Indian trade in 1951.

Claim for the assessment years 1952-53 to 19-54-55.

(2) S. S. Billiton Brought into use in 1951. Brought into use in the Indian trade in 1952. Claim for the Assessment years 1953-54 to 1956-57.

(3) S, S. Banka Brought into use in 1953. Brought into use in the Indian trade in 1954. Claim for the assessment years 1955-56 and 1956-57.

(4) S. S. Bawean Brought into use in 1953. Brought into use in the Indian trade in 1954. Claim for the assessment years 1955-56 and 1956-57."

The assessee and the Commissioner were agreed that the taxable income of the assessee had to be determined by the application of the second method in Rule 33 of the Indian Income-tax Rules, 1922. The Tribunal also observed that the Commissioner and the assessee agreed that the formula adopted by the Income-tax Officer was "the correct method of assessment".

The Commissioner submitted before the Tribunal that if the Indian business of the assessee be regarded as part of its world business and not independent of it, the world profits of the assessee must be computed according to the provisions of the Indian Income-tax Act, 1922, and additional depreciation may be taken into account in determining the taxable profits under the Indian Income-tax Act as a fraction of the world profits. But he maintained that if the Indian trade be regarded as a separate business and not part of the world trade of the assessee, additional depreciation could only be allowed under S. 10(2)(vi-a) of the Indian Income-tax Act, provided ships which are new are introduced into the Indian trade and not otherwise, In the opinion of the Tribunal, in computing the taxable in- come of the assessee under the Indian Income-tax Act, 1922, the Indian business must be taken to be part of the assessee's world business, and "depreciation which the assessee was entitled to, in respect of its world business by the application of the Indian Income-tax Act would be proportionately available in respect of its Indian business." The Tribunal observed that under r. 33 "the profits have to be calculated under the terms of the Indian Incometax Act and this act postulated that on all machinery, plants and such other things like steamers brought into business after March 31, 1948, additional depreciation must also be granted". The Tribunal then observed that the ships brought into the Indian trade were not new in the years of account relevant to the five years of assessment, but the assessee was still qualified under S. 10(2) (vi-a) to additional depreciation for a continuous period of five years, and "the fact in the first of these years the new ships did not call at the Indian Ports in one assessment year did not disentitle the assessee to the benefit not only for that year but also for the succeeding four years". Accordingly the Tribunal held that in respect of all the four ships of the assessee, additional depreciation was admissible as claimed. At the instance of the Commissioner of Income-tax, the fol- lowing question was referred

by the Tribunal to the High Court of Calcutta for opinion in respect of each of the five years :

> "Whether on the facts and circumstances of the case the assessee-Company is entitled to additional depreciation in respect of the four ships mentioned above?"

The High Court answered the question in the negative Clause (vi-a) was inserted in s. 10(2) of the Indian Income- tax Act, 1922, by s. 11 of the Taxation Laws (Extension to Merged States and Amendment) Act 67 of 1949. The clause as amended by s. 8 of the Indian Income-tax (Amendment) Act 25 of' 1953 with effect from April 1, 1952, reads as follows :

> "In respect of depreciation of buildings newly erected, or of machinery or plant being new which has been installed, after the 31st day of March, 1948, a further sum (which shall be deductible in determining the written down value) equal to the amount admissible under clause (vi) (exclusive of the extra allowance for double or multiple shift working of the machinery or plant and the initial depreciation allowance admissible under that clause for the first year of erection of the building or the installation of the machinery or plant) in not more than five successive assessments for the financial years next following the previous year in which such buildings are erected and such machinery and plant installed and falling within the period commencing on the 1st day of April, 1 949, and ending on the 31st day of March, 1959."

The assessee is a non-resident Company. It maintains a Branch Office in Calcutta; but on that account the' Indian business of the assessee cannot be regarded as business distinct from its world business. It was not so treated by the Income-tax Officer, or by the Appellate Assistant Commissioner. In computing profits or gains of business carried on by an assessee, normal depreciation under, S. 10(2)(vi) and additional depreciation under S. 10(2)(vi-a) are undoubtedly admissible in the conditions and to the extent allowed under the two clauses. By S. 4(1) of the Indian Income-tax Act, the total income of any previous year of a non-resident includes all income, profits and gains from whatever source derived which- (1) are received or are deemed to be received in the tax- able territories in such year by or on behalf of such person, and (2) which accrue or arise or are deemed to accrue or arise to him 'in the taxable territories during such year. Section 10 of the Act which charges to tax the profits and gains of business, profession or vocation carried on by an assessee applies to assessees who are residents, residents but not ordinarily resident, and non-residents. Profits and gains of business of a non-resident received or deemed to be received in the taxable territories by or on behalf of the assessee are taxable under the Indian Income Tax Act 1922 :

> profits and-gains of business which accrue or arise or are deemed to accrue or arise to him in the taxable territories are also taxable under that Act; but profits and gains which accrue or arise or are deemed to accrue or arise to a non- resident without the taxable territories are not taxable under the Act.

Section 4 is one of the pivotal sections in the scheme of the Income-tax Act. Thereby within the total income of a non-resident is included income received, arising or accruing, or deemed to be received, or to have arisen or accrued, -within the taxable territories. The Act however gives no clear guidance for determining when income may be said to have arisen or accrued within the taxable territories. But r. 33 framed under the Act purports to give some direction to the Income-tax Officer for determining income, profits or gains accruing or arising to a non-resident for the purpose of assessment to income-tax. There is no dispute that the profits of the business taxable under the Indian Income-tax Act, 1922, are a fraction of the world-profits-and the profits are to be determined under r. 33 of the Income-tax Rules. Rule 33 of the Income-tax Rules reads as follows :

"In any case in which the Income-tax officer is of Opinion that the actual amount of the income, profits or gains accruing or arising to any person residing out of the taxable territories whether directly or indirectly through or from any business connection in the taxable territories or-through or from any Property in the taxable territories, or through or from any asset or, source of income in the taxable territories, or through or from any money lent at interest and brought into the taxable territories in cash or in kind cannot be ascertained, the amount of such income, profits or gains for the purposes of assessment to income-tax may be calculated on such percentage, of the turnover so accruing or arising as the Income-tax Officer may consider to be reasonable, or on an amount which bears the same proportion to the total profits of the business of such person (such profits being computed in accordance with the provisions of the Indian Income-tax Act) as the receipts so accruing or arising bear to the total receipts of the business, or in such other manner as the Income-tax Officer may deem suitable."

The rule authorises the Income-tax Officer to adopt one of the three methods of determining income, profits or gains'- ?Or the purpose of assessment to income-tax where the Income-tax Officer is unable to ascertain the actual amount of income, profits or gains, arising inter-alia out of a business connection in the taxable territories :-(a) a percentage of turnover considered reasonable (b) a proportion of the total profits (computed according to the provisions of the Indian Income Tax Act) of the business of the assessee equal to the proportion which the receipts accruing or arising bear to the total receipts of the business and (c) such other manner as the Income-tax Officer may deem suitable.

The second method, it was common ground, was properly applicable to the determination of taxable income of the assessee. That method requires as a first step, determination of the total profits of the business of the assessee in accordance with the provisions of the Indian Income-tax Act: the next step is to determine the proportion between the receipts accruing or arising within the taxable territories and the total -receipts of the business; and the third step is to determine the income, profits or gains by the application of the proportion for the purpose of assessment to income-tax. This method ordains that the fraction which the total profits bear to the total world receipts is to be applied to the Indian receipts for determining the taxable profits. The income so determined will be

the taxable income without any further allowances, because the permissible allowance will all -enter the computation of the world income and income taxable under the Income-tax Act is also a fraction thereof. Apparently the Income-tax Officer did not apply the second method under r. 33 in computing the taxable income of the assessee, for under that method in determining the taxable income the receipts accrued or arising in India had to be multiplied by the proportion between the total profits of the business and the total receipts of the world business.

Counsel for the assessee asked us to assume that the profits computed by the Income-tax Officer according to the formula adopted by him are profits determined by the second method in r. 33, and claimed on that footing that beside normal depreciation, additional depreciation ought also to have been taken into account, and the taxable profits of the assessee determined on that basis. But that assumption cannot be made. One of the essential conditions of the applicability of the second method in r. 33 is the determination of the total world profits of the assessee under the Indian Income-tax-Act, and reduction of the Indian taxable profits by the application of the appropriate fraction. The assessee has not produced its books of account of its world trade to enable the Income-tax Officer to determine its total taxable profits arising from its world business.

There was apparently no clear appreciation of the true im- port of the second method under r. 33 before the Departmental Authorities and the Tribunal. Counsel for the assessee suggested that his client may be willing to produce before the Income-tax Officer the books of account of the relevant years for computing the total world profits according to the Indian Income-tax Act, 1922, and the benefit of additional depreciation may then be allowed to the assessee in computing the total profits under the Indian Income-tax Act. Counsel for the Commissioner expressed his willingness to the adoption of that course. Counsel requested us to adjourn the hearing to enable them to obtain instructions from their respective clients, and the hearing was accordingly adjourned for three weeks. But ultimately counsel for the assessee informed us that his clients may not be able to bring before the Income-tax Officer the books of account of their world trade.

The Income-tax Officer has evolved a special formula for de- termining the profits which is not the second method in r. 33 of' the Income-tax Rules. The assessee has not challenged the correctness of that method, nor has the Department. In the application of that formula, normal depreciation and trade expenses are deducted from the total gross earning in the Indian trade, but not the additional depreciation.

Clearly the Income-tax Officer did not in computing the tax- able income resort to the second method in r. 33 of the Incometax Rules. We are exercising in these appeals advisory jurisdiction, and are only called upon to answer the question referred by the Tribunal. We are incompetent to decide whether computation of the taxable income by the Income-tax Officer by the application of the formula evolved by him is correct: that question is not before us. We are only concerned to determine the validity of the claim for admitting additional depreciation in the computation of the taxable income of the assessee by the method -adopted by the Income-tax officer. Additional depreciation is a statutory allowance in the determination of taxable profit under S. 10 of the Act, and in the case of a non-resident where actual income cannot be determined, and resort is had to r. 33, not when an empirical method is adopted for computation of the tax-able income.

We are however unable to agree with the observations of the High Court that "no relief in any shape or form can be enjoyed by any assessee under the Indian Income-tax Act in respect of a source of income, unless the income from that source is taken into consideration for the purpose of that Act. In the reference before us the income in question was outside the purview of assessment under the Indian Income- tax Act". That was not the plea of the Commissioner. The source of the income of the assessee charged to tax was business: it was not income from any other source. The Commissioner and the assessee were ad idem on that matter. The only dispute was whether additional depreciation was admissible in the computation of the taxable income, when the taxable business profits were determined by the Income- tax Officer by the method evolved by him.

It was common ground that the appropriate method for deter- mining the profits was the second method in r. 33. But that method was never applied: if it was applied in the computation of the world profits of the assessee, it would have been necessary to allow the various depreciation allowances. The assessee could not, while accepting determination of taxable profits in a manner not warranted by the second method under r. 33, claim that additional depreciation should be allowed. The answer to the question therefore is that additional depreciation is not admissible as an allowance in the computation of the taxable income by the special formula adopted by the Income-tax Officer. The appeals fail. The assessee will pay the costs of these appeals. One hearing fee.

R.K.P.S. Appeals dismissed.