

Commissioner of Income-Tax, Bombay City

Vs

M. K. Kirtikar

Civil Appeal No. 7 of 1958

(CJI S. R. Dass, N. H. Bhagwati, M. Hidayatullah JJ)

07.05.1959

JUDGMENT

DAS, C.J. -

This is an appeal by special leave from the order of the High Court of judicature at Bombay passed on September 22, 1955, on a reference under section 66(I) of the Indian Income-tax Act (XI of 1922, hereinafter referred to as "the said Act") made by the Income- tax Appellate Tribunal whereby the High Court answered the question of law referred to it by the Tribunal in the affirmative.

The respondent was an employee of Dadajee Dhackjee and Co., Bombay (hereinafter referred to as "the firm"). The firm used to pay to each of its three employees, including the respondent, a commission of one per cent. On its total annual turnover in its Colour Department in addition to their respective salaries. In connection with the assessment of the firm's income for the assessment year 1945-46, for which the accounting year was Sambat 2000 (covering the period between October 30, 1943, to October 17, 1944), the Income-tax Officer found that the profit and loss account of the Colour Department of the firm had been debited with Rs. 84,540 as and by way of commission paid to three employees of the firm including the respondent, the commission being calculated at three per cent. On the annual turnover of that department, i.e., at one per cent in respect of each of the per cent. to those three employees in the preceding accounting year., Sambat 1999, and in the assessment for the corresponding assessment year 1

On March 19, 1949, the respondent submitted returns for the assessment years 1944-45, 1945-46, 1946-47, 1947-48 and 1948-49. In connection with the assessment years 1944-45 and 1945-46, the respondent claimed that, as in the assessment of the firm during the years 1944-45 and 1945-46 two-thirds of the commission paid to him for Sambat years 1999 and 2000 had been disallowed and taxed in the hands of the firm, he was entitled to an exemption from income-tax and super-tax on the commission so disallowed to the firm and on which the firm had paid the tax. As already stated the respondent's share of commission disallowed to the firm in respect of the assessment year 1945-46 was Rs. 18,787. This claim was made on the strength of the Finance Department Notification NO. 878-F dated March 21, 1922, as amended by Notification No. 8 dated March 24, 1928. The said notification was expressed in the terms following :

"The following classes of income shall be exempt from the tax payable under the said Act, but shall be taken into account in determining the total income of an assessee for the purposes of said Act :

(1) Sums received by an assessee on account of salary, bonus, commission or other

remuneration for services rendered or in lieu of interest on money advanced to a person for the purposes of his business,

Where such sums have been paid out of, or determined with reference to, the profits of such business and by reason of such mode of payment or determination, have not been allowed as a deduction but have been included in the profits of the business on which income-tax has been assessed and charged under the head 'business.

Provided that such sums shall not be exempt from the payment of super-tax unless they are paid to the assessee by a person other than a company and have already been assessed to super-tax."

The Income-tax Officer rejected this claim and his decision was upheld on appeal by the Appellate Assistant Commissioner. A further appeal to the Tribunal was also rejected, the Tribunal taking the view that the notification could only apply in respect of the profits of a business on which income-tax had been assessed and charged and that as the income of the firm had not been assessed and charged to income-tax in the relevant year, the notification had no application.

On application under section 66(I) of the said Act, the Tribunal, on January 14, 1955, submitted a statement of case to the High Court raising the following question of law for the determination of the High Court :

"Whether the assessee is entitled to relief granted by the Notification referred to above ?"

The High Court answered the referred question in the affirmative, i.e., in favor of the assessee respondent. In doing so, the High Court repelled both the contentions of the learned Advocate-General appearing for the Department, namely, that the commission had not been paid out of the profits and that income-tax had not been assessed and charged on the income. According to the High Court, the order of assessment clearly showed that the commission had been paid out of the profits and that, as on computation the amount of Income was assessable, it became immediately liable to tax under section 3 and was, therefor, statutorily charged to tax. The High Court having refused to grant a certificate of fitness for appeal to this court, the Commissioner of income-tax, Bombay, applied for and obtained from this court special leave under article 136 of the Constitution to appeal to this court. The short and simple question in this appeal is whether, on a true construction of the notification, the respondent is entitled

A perusal of the notification clearly indicates that exemption from taxation in respect of the sum received by an assessee from a business on account, inter alia, of commission can be claimed only on three conditions, namely :

- "(1) Where such sum has been paid out of or determined with reference to the profits of the business;
- (2) Where by reason of such mode of payment or determination the sum paid has not been allowed as a deduction but has been included in the profits of the business; and
- (3) Where on the sum so disallowed in the computation of the profits of the business, income-tax has been assessed and charged under the head 'business.'"

These three conditions are cumulative and all of them have to be fulfilled before the assessee can claim the benefit of exemption. The obvious purpose of this notification is to avoid double taxation by providing that if the amount in question has been assessed and charged in the hands of the firm, the same should not be assessed and charged over again in the hands of the assessee.

As regards the first condition it is clear that the commission had not determined with reference to the profits of the business of the firm, for it was agreed to be calculated at a given percentage of the total turnover of the year. The only question, for the purpose of this condition, is whether the commission had been paid out of the profits. The Department points out that according to the profit and loss account of the Colour Department of the firm the profit was shown as Rs. 4,27,139 and that sum having been arrived at after the payment of salary, commission and other outgoing, it cannot possibly be said that the commission had been paid out of the profits, for profits could only be ascertained after the outgoing had been paid. In support of the order of the High Court, the respondent maintains that the profit had been found to have been understated because the net profit, as shown in the order of assessment, was really Rs. 5,30,900. As this real profit has been reduced to Rs. 4,27,139 only by debiting th

The second condition, which appears not to have been noticed by the High Court, is that the sum paid out of profits of determined with reference to the profits of the business had not been allowed as a deduction "by reason of such mode of payment or determination". In this case learned counsel for the Department urges, the amount was disallowed not because it had been paid out of profits or had been determined with reference to the profits of the business, but because he held it to be excessive and unnecessary and not a permissible deduction under section 10(2)(xv) of the said Act. There is good deal to be said for view. But here, again, the matter does not appear to have been raised either before the matter does not appear to have been raised either before the Income-tax authorities or the High Court and we cannot, therefore, base our decision on this ground.

The third condition for successfully claiming relief under the notification is that income-tax should be shown to have been "assessed and charged under the head business" on the sum paid as commission but not allowed as a deduction. In ascertaining the meaning of the word "charged", the High Court has referred to what have been described as the four processes recognized by the Income-tax Act, namely, (i) assessment, meaning the mode of computation, (ii) the levy, which is the procedure laid down for the realization of the tax, and (iv) the actual payment. The High Court has placed reliance on section 55 of the said Act where the words "charged, levied and paid" have been used in connection with the payment of super-tax. This does not appear to us to be the right approach. What is to be ascertained is the meaning of the word "charge" as used in the notification under consideration. It is clear that the primary object and purpose of the notification is to prevent double taxation on the same amount, namely, onc

For the reasons stated above the referred question in our opinion be answered in the negative. The appeal is therefore allowed with costs both here and in the court below.

Appeal allowed.

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