

War Profits Tax Commissioner

Vs

Binodiram Balchand

Civil Appeal No. 225 of 1960

(P. B. Gajendragadkar, A. K. Sarkar, K. N. Wanchoo, N. Rajgopala Ayyangar, K. C. Das Gupta JJ)

20.12.1961

JUDGMENT

AYYANGAR J. –

This appeal comes before us by virtue of a certificate of fitness granted by the High Court of Madhya Pradesh under section 47 (2) of the Gwalior War Profit Ordinance, Samvat 2001 (hereafter called the Ordinance) on the ground that the appeal involves a substantial question of law.

The question of law which arises in the appeal relates to the proper construction of rule 3 (1) of the schedule of the Ordinance. The respondent - M/s. Binodiram Balchand is the name under which a Hindu undivided family which was resident in the State of Gwalior carried on various businesses in that State. Profits derived from business carried on the State were charged to war profits tax under the Ordinance. Among the businesses carried on by the respondent was its employment as the secretary, treasurer and managing-agent of a textile mill which was a limited company bearing the name of Binod Mills Company Limited, Ujjain. The appeal is concerned with the computation of the profits of the respondent to war profits tax under the Ordinance, which, it might be state at the outset, was on lines very similar to the Indian Excess Profits Tax Act, 1940.

The chargeable accounting period with which the appeal is concerned, is the period commencing from July 1, 1944, to October 16, 1944. The respondent assessee submitted its return and thereafter the War Profits Tax Officer by his assessment order dated July 9, 1951, determined the taxable income of the assessee for this chargeable accounting period at Rs. 12,16,145 and assessed it to tax in the sum of Rs. 2,02,691. Several points were raised in relation to this assessment order by the respondent, and one of them related to the inclusion in its assessable profits of a sum of Rs. 11,09,332 which was received by the respondent on July 5, 1944, being the dividend declared and paid by the Binod Mills Ltd. for 1943 on the shares held by the respondent. It was the contention of the respondent that this sum was its income from an investment pure and simple and was not "profits" from business, and so could not be included in its taxable profits on a proper construction of the relevant provisions of the Ordinance. From

"46. (1) If, in the course of any assessment under this Ordinance or any proceeding in connection therewith, a question of law arises, the Commissioner, may, either on his own motion or on reference from any war profits tax authority subordinate to him, draw up a statement of the case and refer it with his own opinion thereon to the High Court."

The Commissioner acceded to this request and referred for the opinion of the High Court three

questions :

"(i) Whether the dividend income of Rs. 11,09,332 received from the Binod Mills was chargeable under the War Profits Tax Ordinance ?

(2) Whether certain bad debts written off by the assessee could be allowed deductions in computing profits for war tax purpose ?

(3) Whether the expenses of assessee's branch at Gwalior which was defunct, could be allowed as admissible expenses ?"

The High Court answered questions Nos. 2 and 3 in favour of the department, but the first question was answered in the negative and in favour of the assessee. There is now no dispute as regards questions 2 and 3 and the appeal is confined to the correctness of the answer to the first question.

Before setting out the grounds upon which the High Court decided the reference in favour of the respondent it is necessary to read a few of the provisions of the relevant law which bear upon the point arising for consideration. The preamble to the Ordinance recites that it was enacted to impose a tax on "excess profits arising out of certain businesses" and this intention is carried out by section 4 (1) which is the charging section which enacts :

"4. (1) Subject to the provisions of this Ordinance, applies, be charged, levied and paid on the amount by which the profits during any chargeable period exceed the standard profits, an excess profits tax (in this Ordinance referred to as the 'war profits tax') which shall be equal to 60 per cent. of aforesaid amount."

The expression "business", the profits derived from which are thus brought to charge is defined by section 2 (5) in these terms :

"2. (5) 'business' includes any trade, commerce or manufacture or any adventure in the nature of trade, commerce or manufacture or any profession or vocation, but does not include a profession carried on by an individual in partnership, if the profits of the profession depend wholly or mainly on his or their personal qualifications, unless such profession consists wholly or mainly in the making of contracts on behalf of other persons or the giving to other persons of advice of a commercial nature in connection with the making of contracts :

Provided that where the functions of a company or of a society incorporated by or under any enactment consists wholly or mainly in the holding of investments or other property or both, the holding thereof shall be deemed for the purpose of this definition to be a business carried on by such company or society :

Provided further that all businesses to which this Ordinance applies carried on by the same person shall be treated as one business for the purposes of this Ordinance."

There are two further definitions which are of some relevance to the arguments addressed to us and might therefore be set out at this stage. Section 2 (14) defines the expression "prescribed" as meaning "prescribed by rules made under the Ordinance;" section 50 being the provision empowering the Government to make rules and this section ran :

"50. (1) Subject to the provisions of this Ordinance, Government may make rules for carrying out the purposes of this ordinance.

(2) Rules made under this section shall be published in the Official Gazette and shall thereupon have effect as if enacted in this Ordinance."

The other relevant definition is of the expression "profits" which is defined in section 2 (16) as :

"profits as determined in accordance with the provisions of this Ordinance and its first Schedule."

There is a first schedule which follows the Ordinance and which is headed 'Rules for the computation of profits for the purposes of war profits tax', and of these the one pertinent to the matter in controversy in the appeal is rule 3 of which sub-rules (1) and (2) have been relied on in the course of arguments.

They run :

"3. (1) Income received from investments shall be included in the profits of a business liable to the war profits tax, unless it is proved to the satisfaction of the War Profits Tax Officer that the investments have no connection whatever with the business.

(2) In the case of a business which consists wholly or mainly on the dealing in or holding of investments, income received from investments shall be deemed to be profits of that business, and in the case of a business, a specific part only of which consists in dealing in investments, the income received from investments held for the purposes of that part of the business shall be deemed to be profits of that part of the business.

Explanation. - 'The income from investments to be included in the profits of the business under the provisions of this rule shall be computed exclusive of all income received by way of dividends or distribution of profits from a company carrying on a business, to the whole of which the section of the Ordinance imposing the war profits tax applies'."

Pausing here, it is necessary to mention that in relation to the first question regarding the inclusion of the dividend income in the taxable profits of the assessee three contentions were raised on behalf of the respondent which are thus set out in the judgment under appeal :

"(1) The assessee did not deal in shares and their holdings in the Binod Mills Limited were purely in the nature of investments, having no connections with their business as defined in section 2 (5) read with rule 1 of schedule I of the Gwalior War Profits Tax Ordinance. The business of the secretaries, treasurers and agents of the Binod Mills Limited, which was carried on by them did not require any holding of the shares of the company and was not dependent on their investment in the said company.

(2) The dividend income accrued or arose from the profits of the Binod Mills Limited, and as the Ordinance applied to the business carried on by this company, the

dividends were excluded under the Explanation to rule 3 (1) of schedule I.

(3) The dividend income should be considered as income of the full accounting period, i.e., from Diwali of 1943 to Diwali of 1944, and should be apportioned on that basis."

The learned judges of the High Court dealt only with the first of the above contentions, and, having accepted it, considered it unnecessary to express any opinion on the other two.

We may now proceed to state the grounds upon which the learned judges of the High Court answered this contention in favour of the respondent. It was urged before them by the respondent that though the provisions headed "Rules for the computation of business" purported to be part of the Ordinance itself as forming the schedule to the Ordinance, they were in reality rules made by Government under the rule-making power conferred on it by section 50 of the Ordinance. This argument was accepted apparently being aided by the fact that immediately after the title "Schedule" occur the words "(See section 2 (14))". Proceeding on this charge under section 4 (1) was on the profits of a business and unless an activity which resulted in any income derived was one in the nature of trade, the mere fact that income was derived therefrom would not make it assessable to tax under Ordinance. This they deduced from an interpretation of the words used in the charging section read in conjunction with the definition of "profits" i

Mr. Sen, learned counsel for the appellant has, however, placed before us material to show that Schedule I containing the rules for the computation of profits were not rules made by the Government under section 50 of the Ordinance but was really part of the Ordinance itself. In the first place, it has to be noted that section 2 (16) speaks of Schedule I to the Ordinance, and admittedly besides the one now produced before us there was no other Schedule attached to the Ordinance. It is impossible to hold that with section 2 (16) in the form in which we now find it, the rules for the computation of the business did not form part of the Ordinance having been enacted simultaneously as part and parcel thereof. In this connection it might be pointed out that the Excess Profits Tax Act, 1940, which formed the basis or model upon which the Ordinance was fashioned has a similar Schedule headed "Rules for the computation of profits" and the Schedule formed part of that Act. The only ground for even a suspicion that Sch

"In exercise of the powers conferred by section 50 of the War Profits Tax Ordinance the Government of Gwalior are pleased to make the following rules..."

It is obvious therefore that "section 2 (14)" in Schedule I is a mistake or a misprint for "section 2 (16)" and it might be noted that in the corresponding Schedule to the Indian Excess Profits Tax Act, 1940, immediately after the title "Schedule I" occur the words "See section 2 (19)" which in that enactment corresponds to section 2 (16) of the Ordinance.

There are other circumstances to which Mr. Sen has drawn our attention which also point to the Schedule being part of the Ordinance and not rules made under it under section 50. The Schedule was the subject of amendments more than once and each time this was done it is significant that this was done not by virtue of the exercise of the rule-making power under section 50 of the Ordinance but by further ordinances showing clearly that the Schedule was part of the Ordinance itself. To give just a few examples, the Explanation to rule 3 (2) which we have extracted earlier was not in the Schedule as originally enacted but was introduced as an amendment by Ordinance No. 42 dated February 28, 1946. The short title of this Ordinance runs :

"This Ordinance might be called the Gwalior War Profits Tax (Amendment) Act, Samvat 2002".

Further it would be noticed that in the Explanation there is a comma after the words "carrying on a business". That comma was not there when the schedule was amended by the Amending Ordinance of February 28, 1946, but was introduced by Ordinance 5 of Samvat 2004 and the short title of this second Ordinance reads :

"This Ordinance might be called the Gwalior War Profits Tax (Amendment) Ordinance Samvat 2004".

We do not consider it necessary to dilate on the point as we are clearly of the opinion that the Schedule was part of the Ordinance and has therefore to be read not as subordinate legislation under rule 50 but as part and parcel of the Ordinance itself.

The whole basis therefore of the reasoning upon which the learned judges of the High Court proceeded falls to the ground and the only question is whether accepting the respondent's case that the shares held by it in the Binod Mills Ltd. were really part of its investments, these investments have "any connection" with its business. It is common ground that the respondent was the secretary, treasurer and managing agent of the Binod Mills and what we are now concerned with are the shares held by it in that company. In the case of every assessee who carries on a business activity and is in receipt of profits from that business, on the terms of rule 3 (1) income from every investment held by him is liable to be included in the profits assessable to tax unless such person was able to satisfy the revenue authorities that the investments "no connection whatever" with his business. Mr. Viswanatha Sastri, learned counsel for the respondent, sought to overcome this position by submitting that the "connection" contempla

We are therefore of the opinion that the dividend received by the respondent from the Binod Mills Ltd. was properly included by the assessing authorities in the computation of the taxable profit of the respondent under the Ordinance and that the High Court erred in answering the reference in favour of the assessee. We have already pointed out that the High Court did not deal with or express any opinion on the two subsidiary contentions urged by the respondent with reference to the first question. Those points were also naturally not argued before us and we do not express any opinion on them. It is obvious that the reference cannot be disposed of without deciding these contentions and the case would have to be remanded to the High Court for dealing with these subsidiary points.

The appeal will accordingly be allowed, the judgment of the High Court set aside and the first contention in relation to question No. 1 answered against the assessee and in favour of the appellant and the case remanded to the High Court for the consideration of the other contentions with reference to that question. The appellant will be entitled to his costs here. The costs in the High Court will be provided in its final order.

Appeal allowed and case remanded.

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