Union of India and Others

Vs

Coromandel Fertilizers Ltd. and Another

Civil Appeals Nos. 969-972 of 1975

(K. K. Mathew, Syed M. Fazal Ali JJ)

09.12.1975

JUDGMENT

GOSWAMI, J. -

1. An important question of law as to the interpretation of Section 80K of the Income-tax Act, 1961 (briefly the Act), is raised in these four appeals by special leave.

2. M/s. Coromandel Fertilizers Ltd. (first respondent) is a registered company incorporated on October 16, 1961, under the Companies Act and the second respondent is one of its shareholders holding two hundred equity shares in the paid-up capital of the company out of a total number of 95,82,010 equity shares issued by it. The company was engaged in manufacture of fertilisers at its factory at Vishakhapatnam and it commenced production in December, 1967.

3. There is no dispute that the company as such fulfilled the appropriate conditions laid down under sub-section (1) of Section 80J of the Act to qualify for deduction in respect of profits up to an extent of six per cent. per annum on the capital employed in respect of profit for the purpose of computation of tax.

4. The company was assessed to income-tax as an industrial undertaking for the first time for the assessment year 1969-70. The orders of assessment were passed on November 23, 1972, and January 4, 1973. The said orders disclosed a sum of Rs. 11,10,176, being carried forward as unabsorbed losses to the succeeding year and a sum of Rs. 9,73,93,861, being carried forward as unabsorbed depreciation to the subsequent year.

5. The capital employed by the company in its new industrial undertaking was Rs. 48,87,38,018, and 6% thereof under section 80J(1) amounted to Rs. 2,93,24,281. Out of this amount, the amount relating to the ten months of the year confined to the period during which the industrial undertaking was in operation was determined by the Income-tax Officer at Rs. 2,44,96,901. As no profit was made in the assessment year 1969-70 the aforesaid "deficiency" within the meaning of Section 80J(3) was carried forward to the succeeding year 1970-71. Similarly for the next assessment year 1970-71 it was recorded in the assessment order that the company was entitled to deduction of Rs. 2,58,31,806 under Section 80J. As there were no profits to be absorbed, the said amount has been carried forward under Section 80J(3) to the succeeding assessment year 1971-72. The returns filed for the assessment year 1971-72 by the company have not been finalised. But all the same the company, as per its books, and had made a profit of Rs. 4.55 crores approximately in the accounting year 1972 corresponding to the assessment year 1973-74. It does not appear to be disputed that for the assessment year 1973-74, the company's income after deducting depreciation for that year would

come to Rs. 6.16 crores. This amount would be subject to set-off against unabsorbed depreciation and business losses which would exceed the said Rs. 6.16 crores resulting in nil total income with some unabsorbed depreciation and business loss to be carried forward to the next assessment year 1974-75. It is not disputed that after setting off the brought-forward allowances the company will not be assessable to any income-tax upto the assessment year 1973-74.

6. The company made business profit of Rs. 4.55 crores in the year 1972. The Board of Directors at their meeting held on March 14, 1973, recommended declaration of a maiden dividend of Rs. 76,66,608 out of the profits of that year. The company represented to the Income-tax Officer on March 3, 1973, seeking a certificate under Section 197(3) of the Act pointing out that the dividend payable by it would qualify for deduction in the hands of the shareholders under Section 80K of the Act. The company sought permission of the Income-tax Officer not to deduct tax at source out of the dividend payable to the shareholders. The request of the company was rejected by the Income-tax Officer holding that the shareholders were not entitled to the benefit of Section 80K of the Act. On coming to know about the declaration of the dividend by the company, even the respondent-shareholder had also requested the company to obtain the necessary certificate. The refusal of their request led to the institution of writ applications by the respondents before the High Court of Andhra Pradesh.

7. According to the High Court the shareholders are entitled to claim deduction under Section 80K of the Act and the company was entitled to an order of the Income-tax Officer under section 197(3) for issuing a certificate enabling it not to deduct tax out of the dividend payable to the shareholders.

8. It is submitted on behalf of the appellants that the question raised is governed by a decision of this court in C.I.T., Madras v. S. S. Sivan Pillai ((1970) 77 ITR 354 : (1970) 2 SCC 180). In that case this Court was required to consider the provisions of Section 15C of the Income-tax Act, 1922 (briefly the old Act) which was largely different from the present sections with which we are concerned in these appeals. The assessment years that came up for consideration in that decision were 1954-55 and 1955-56.

9. It may be appropriate to set out Section 15C :

> 15C. Exemption from tax of newly established Industrial Undertakings: - (1) Save as otherwise herein provided, the tax shall not be payable by an assessee on so much of the profits or gains derived from any industrial undertaking (or hotel) to which this section applies as do not exceed six per cent, per annum on the capital employed in the undertaking (or hotel), computed in accordance with such rules as may be made in this behalf by the Central Board of Revenue.

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> (4) The tax shall not be payable by a shareholder in respect of so much of any dividend paid or deemed to be paid to him by an industrial undertaking (or a hotel) as is attributable to that part of the profits or gains on which the tax is not payable under this section.

Explanation : - The amount of dividend in respect of which the tax is not payable under this sub-section shall be computed in accordance with such rules as may be made in this behalf by the Central Board of Revenue.

10. While dealing with the above section this court observed in C.I.T. v. S. S. Sivan Pillai as under :

Exemption under Section 15C(1) from payment of income-tax is not related to the business profits; it is related to the taxable profits. The language of sub-section (3) is clear; the profits or gains of an industrial undertaking have to be determined under Section 10 of the Act. Even if the undertaking has earned profits out of its commercial activity, if it has no taxable profits it cannot claim exemption from payment of tax under sub-section (1) of Section 15C : and if the undertaking cannot claim the benefit under sub-section (1) the shareholders will not get the benefit of sub-section (4), for there is no dividend paid which is attributable to that part of the profits or gains on which the tax was not payable by the undertaking.

The company had no taxable profit in the year of account; it did not accordingly qualify for exemption from payment of tax under sub-section (1), and since there was no such taxable profit, the dividend received by the shareholders could not be said to be attributable to that part of the profits or gains on which the tax was not payable under sub-section (1). On the plain terms of Section 15C the shareholders cannot obtain the benefit of exemption from payment of tax. (page 367 of the report)

The right of the shareholders to obtain the benefit of exemption under Section 15C(4) depends upon the company obtaining the benefit of exemption under sub-section (1) of Section 15C, for the exemption from payment of tax on the dividend received by the shareholders is admissible only on that part of the profits or gains on which the tax is not payable by the company under sub-section (1). (page 359 of the report)

11. As will be shown later this decision will not be of aid to the appellants in view of the changes in the law.

12. With a view to offer incentive to investment, Section 15C of the old Act was dealing with the principle of truce with tax for a limited period or what is described as tax-holiday benefit with which we are concerned. The finance (No. 2) Act of 1967 substituted the earlier provisions in that behalf in Chapter VI-A in the Income-tax Act, 1961 with effect from April 1, 1968. We will, therefore, read the provisions of the material section in this chapter, namely, sub-sections (1) and (3) of Section 80J and Section 80K :

> 80J(1). Where the gross total income of an assessee includes any profits and gains derived from an industrial undertaking or a ship or the business of a hotel, to which this section applies, there shall, in accordance with and subject to the provisions of this section, be allowed, in computing the total income of the assessee, a deduction from such profits and gains (reduced by the aggregate of the deductions, if any, admissible to the assessee under Section 80H and Section 80I) of so much of the amount thereof as does not exceed the amount calculated at the rate of six per cent. per annum on the capital employed in the industrial undertaking or ship or business of the hotel, as the case may be, computed in the prescribed manner in respect of the previous year relevant to the assessment year (the amount calculated as aforesaid being hereafter, in this section, referred to as the relevant amount of capital employed during the previous year).
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> (3) Where the amount of the profits and gains derived from the industrial undertaking or ship or business of the hotel, as the case may be, included in the total

income [as computed without applying the provisions of Section 64 and before making any deduction under Chapter VI-A or Section 280(O)] in respect of the previous year relevant to an assessment year commencing on or after the 1st day of April, 1967 (not being an assessment year prior to the initial assessment year or subsequent to the fourth assessment year as reckoned from the end of the initial assessment year) falls short of the relevant amount of capital employed during the previous year, the amount of such shortfall, or, where there are no such profits and gains, and amount equal to the relevant amount of capital employed during the previous year (such amount, in either case, being hereafter, in this section, referred to as deficiency) shall be carried forward and set off against the profits and gains referred to in sub-section (1) [as computed after allowing the deductions, if any, admissible under Section 80H, Section 80-I and the said sub-section (1)] in respect of the previous year relevant to the next following assessment year and, if there are no such profits and gains for that assessment year, or where the deficiency exceeds such profits and gains, the whole or balance of the deficiency as the case may be, shall be set off against such profits and gains for the next following assessment year and if and so far as such deficiency cannot be wholly so set off, it shall be set off against such profits and gains assessable for the next following assessment year and so on :

Provided that -

(i) in no case shall the deficiency or any part thereof be carried forward beyond the seventh assessment year as reckoned from the end of the initial assessment year,

(ii) where there is more than one deficiency and each such deficiency relates to a different assessment year, the deficiency which relates to an earlier assessment year shall be set off under this sub-section before setting off the deficiency in relation to a later assessment year :

Provided further that in the case of an assessee being a co-operative society, the provisions of this sub-section shall have effect as if for the words "fourth assessment year", the words 'sixth assessment year' had been substituted.

80K. Where the gross total income of an assessee, being the owner of any shares in a company, includes any income by way of dividends paid or deemed to have been paid by the company in respect of such share or shares, there shall, subject to any rules that may be made by the Board in this behalf, be allowed, in computing his total income, a deduction from such income by way of dividends of an amount equal to such part thereof as is attributable to the profits and gains derived by the company from an industrial undertaking or ship or the business of a hotel, on which no tax is payable by the company under this Act for any assessment year commencing prior to the 1st day of April, 1968, or in respect of which the company is entitled to a deduction under Section 80J.

13. A perusal of Sections 80J(3) and 15C would clearly show the difference in the scheme of the two provisions. Broadly speaking, there was no question of "carry forward" from the accounting year to the succeeding year or years the sums allowable under Section 15C. That feature is now permanent in Section 80J in clearly providing that

where there are no such profits and gains, an amount equal to the relevant amount of capital employed during the previous year (viz., the six per cent of the capital employed) ..... shall be

carried forward and set off against profits and gains referred to in sub-section (1) .....

14. There is another vital distinction. While section 15C(4) refers to relief in case of only taxable profits, Section 80K provides that in computing the total income of an assessee whose gross total income includes any income by way of dividends, there shall be allowed in computing his total income a deduction from such income by way of dividends an amount equal to such part thereof as is attributable to profits and gains derived by the company from an industrial undertaking on which no tax is payable by the company under the Act or in respect of which the company is entitled to deduction under Section 80J. The expression "or in respect of which the company is entitled to a deduction under Section 80J" introduces a new concept. There is no legal requirement of a de facto deduction of the amount in question in the particular assessment year. As against actual deduction the company's entitlement to deduction in the relevant year is enough to answer the requirement or Section 80J. Necessarily, therefore, the dividend-earner will also be entitled to invoke Section 80K and obtain pari passu the benefit of the provision.

15. It is submitted on behalf of the appellants that unless there is actual deduction under Section 80J, the shareholder is not entitled to claim benefit under Section 80K. The appellants further contend that Section 80A(2) of the Act is a complete answer to the claim of the respondents. By sub-section (2) of the Section 80A the entire amount of deduction under Chapter VI-A shall not in any case exceed the gross total income of the assessee. It was therefore, submitted that as there were no assessable incomes of the company in the particular years, the question of deduction of the monetary benefit by the shareholder would not arise. We are unable to accept this submission. Under old Section 15C, the shareholder was entitled to relief only when the company was able to get actual deduction. Both were at par. The parity has been sought to be maintained under the amended provisions of Sections 80J and 80K between the company and the shareholder. The company, when becomes entitled to deduction under Section 80J(1), gets it either in that year or by a set-off in subsequent years. If the interpretations which we have put to the new sections were not to hold good, the result will be that the shareholder will be debarred from getting any relief when dividend is declared in a year in which the company because of Section 80A(2) is not able to get actual deduction. The company will reap to advantage of set-off under Section 80J(3) in subsequent years, while the shareholder for the dividend declared in the past, will get no relief under Section 80K. This anomaly is avoided, and the legislature intended to avoid it, by the use of the expression "the company is entitled to a deduction" in Section 80K and on the interpretation we have put above.

16. We are, therefore, clearly of opinion that the company was not required under the law to deduct at source tax from the dividends which they were declaring to the shareholder. The company was entitled to an appropriate certificate from the Income-tax Officer under Section 197(3). The appeals are, therefore, dismissed and the impugned orders are set aside. The company will be entitled to approach the Income-tax Officers for such appropriate certificates under Section 197(3), as may be admissible on proper computation under the relevant rules. There will be no order as to costs.

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