Commissioner of Income-Tax, Bihar

Vs

Sahu Jain Ltd.

Civil Appeals Nos. 761 and 762 of 1973

(P. K. Goswami, Syed M. Fazal Ali JJ)

16.02.1976

JUDGMENT

GOSWAMI J. –

These two appeals by special leave are directed against the common judgment of March 14, 1969, of the Patna High Court in the matter of two references under section 66(1) of the Indian Income-tax Act, 1922, relating to assessment years 1953-54 and 1954-55 of the respondent (hereinafter to be referred to as the company).

The case has a rather chequered history as will appear from the facts narrated below :

> The company at the material time was a private limited company and at the end of the relevant pervious years, namely, August 31, 1952, and August 31, 1953, the shareholding was as follows :

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		Number of shares on 31-8-1952	31-8-1953
1.	Sri Ashok Kumar Jain, Managing Director.	10,000	10,000
2.	Sri R. Sharma, Director	10	10
3.	Sri N. C. Jain, Director	10	10
4.	Sri S. P. Jain	10,000	10,000
5.	Smt. Rama Jain	10,000	10,000
6.	Sri Alok Prakash Jain	10,000	10,000
7.	Rishabh Investment Ltd.	5,000	5,000
8.	Jalmia Jain Co. Ltd.	2,000	2,000
9.	Universal Bank of India Ltd.	980	980
10.	Ashoka Agencies Ltd.	2,000	2,000

50,000	50,000

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Of these shareholder Rama Jain is the wife of S. P. Jain and Alok Prakash Jain and Ashok Kumar Jain are the sons of S. P. Jain and Rama Jain. Ashok Kumar Jain (briefly A. K. Jain), the managing director, attained majority on March 5, 1952, while Alok Prakash Jain was a minor during both the accounting years. The three companies, namely, Rishabh Investments Ltd., Dalmia Jain Co. Ltd., and Universal Bank of India Ltd., are companies to which the provisions of section 23A of the Indian Income-tax Act, 1922 (briefly the Act), prior to its amendment by the Finance Act, 1955, applied. S. P. Jain was the principal shareholder of the Universal Bank of India Ltd., holding 980 shares. Ashoka Agencies Ltd., with 2,000 shares was a company to which admittedly section 23A did not apply. R. Sharma and N. C. Jain being the secretary of S. P. Jain.

The Income-tax Officer by his orders of September 25, 1957 and October 30, 1957, held that section 23A was attracted in the case of the company for both the years. On appeal, the Appellate Assistant Commissioner remanded the matter back to the Income-tax Officer for a finding on certain additional facts. The Income-tax Officer in his remand report submitted certain additional facts to the Appellate Assistant Commissioner who in due course affirmed the orders of the Income-tax Officer. The company appealed to the Income-tax Appellate Tribunal, Bihar, at Patna. The Tribunal allowed the appeal by its order of January 26, 1961(?) and held that section 23A was not applicable to the company in respect of both the assessment years. At the instance of the Commissioner of Income-tax, Bihar, the following question was referred by the Tribunal to the High Court :

> "Whether, on the facts and circumstances of the case, the Tribunal was justified in holding that the provisions of section 23A of the Income- tax Act were not applicable to the assessee-company for the assessment years 1953-54 and 1954-55 ?"

The High Court by its order of December 9, 1965 in view of two decisions of this court, namely, Raghuvanshi Mills Ltd. v. Commissioner of Income-tax decided on December 7, 1960, and Commissioner of Income-tax v. Jubilee Mills Ltd., decided on September 1, 1962, directed the Tribunal to submit a supplementary statement of case to it :

> "Whether, bearing in mind the principles laid down by the Supreme Court in Raghuvanshi Mills Ltd. v. Commissioner of Income-tax and Commissioner of Income-tax v. Jubilee Mills Ltd., Srimati Rama Jain and Sri Ashok Kumar Jain, or either of them could be safely taken to have acted in concert with Sri S. P. Jain during the years in question, in respect of the affairs of the assessee-company ?"
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> The High Court also directed that "the Tribunal may take additional evidence, if it considers it necessary to enable it to state the supplementary case as directed above".

The Tribunal thereafter, after hearing the parties, submitted a supplementary statement of case to the High Court on September 30, 1966. A controversy arose before the Tribunal with regard to entertainment of additional evidence which the revenue wanted to adduce before it, particularly i view of the direction of the High Court, but the Tribunal did not accede to the request and additional

evidence was not received. The matter then came up before the High Court resulting in the impugned order against the revenue. Hence, these two appeals by special leave.

The revenue reiterated its grievance before the High Court about the Tribunal's refusal to entertain additional evidence without success and the matter is no longer in controversy in view of a decision of seven judges of this court in Keshav Mills Ltd. v. Commissioner of Income-tax, affirming the earlier decisions of this court in the case of New Jehangir Vakil Mills Ltd. v. Commissioner of Income-tax and Petlad Turkey Red Dye Works Co. Ltd. v. Commissioner of Income-tax. It is now well-settled that when the Tribunal has disposed of the matter and is preparing a statement of the case either under section 66 (1) or under section 66 (2), there is no scope for any further or additional evidence and the power of the High Court under section 66 (4) can be exercised only in respect of material and evidence which has already been brought on the record.

It was contended on behalf of the revenue before the High Court that the finding of the Tribunal was perverse. Mr. Sen, appearing on behalf of the revenue before us, has fairly and, in our opinion, rightly not pressed this submission before us. Similarly, on behalf of the company, also it was contended before the High Court that there was no principle of law involved in drawing any inference in the cases in answer to the plea of the revenue that the finding whether section 23A was not attracted was a mixed question of law and fact. It is not possible to hole that the question referred to the High Court is not a question of law as undoubtedly on the statement of case an important question of law does arise and the composite reference was competent.

The question that arises for consideration is whether on the facts and circumstances that are established before the Tribunal the company in the two assessment years can escape the reach of section 23A of the Act.

Section 23A prior to its amendment in 1955 and so far as it is material read as follow :

> "23A. Power to assess individual members of certain companies. -
>
> (1) Where the Income-tax Officer is satisfied that in respect of any pervious year the profits and gains distributed as dividends by any company up to the end of the sixth month after its accounts for that previous year are laid before the company in general meeting are less than sixty per cent. of the assessable income of the company of that previous year, as reduced by the amount of Income-tax and super-tax payable by the company in respect thereof he shall, unless he is satisfied that having regard to losses incurred by the company in earlier years or to the smallness of the profit made the payment of a dividend or a larger dividend than that declared would be unreasonable, make with the previous approval of the Inspecting Assistant Commissioner an order in writing that the undistributed portion of the assessable income of the company of that previous year as computed for income-tax purposes and reduced by the amount of income-tax and super-tax payable by the company in respect thereof shall be deemed to have been distributed as dividends amongst the shareholders as at the date of the general meeting aforesaid, and thereupon the proportionate share thereof of each shareholder shall be included in the total income of such shareholder for the purpose of assessing his total income :...
>
> Provided further that this sub-section shall not apply to any company in which the public are substantially interested...

Explanation. - For the purpose of this sub-section, a company shall be deemed to be a company in which the public are substantially interested if shares of the company... carrying not less than twenty- five per cent. of the voting power have been allotted unconditionally to, or acquired unconditionally by, and are at the end of the previous year beneficially held by the public... and if any such shares have in the course of such previous year been the subject of dealings in any stock exchange... or are in fact freely transferable by the holders to other members of the public."

In this case the company did not declare any dividend for the assessment year 1953-54. In the next assessment year 1954-55, only a sum of Rs. 50,000 was distributed as dividend. It is not in dispute that the company had sufficient requisite assessable income out of which sufficient or larger dividend could have been paid. There is no dispute that the payment of an adequate dividend for the first year and larger dividend for the next year would have been at all unreasonable in respect of these two assessment years. The only controversy between the parties is with regard to the exclusion of the company from the application of section 23A in view of the third proviso read with the Explanation. In other words, is the company one in which the public are substantially interested ? It could be so in terms of the Explanation if 25 per cent. shares of the company or more had been allotted unconditionally to, or acquired unconditionally by and are at the end of the previous year beneficially held by the public and if any such shares in the course of such previous year were in fact freely transferable by the holders to other members of the public. It was not in dispute that the shares of the company were in fact freely transferable by the holders to other members of the public. The controversy, therefore, is within a very narrow compass, namely, whether, as stated earlier, the company is one in which the public has 25 per cent. or more shares allotted unconditionally to, or acquired unconditionally by it and are at the end of the previous year beneficially held by it.

It may be mentioned that section 23A (1), as it stood before the amendment by the Finance Act, 1955, did not authorise amalgamation of the shares held by "relatives" as if they represented a single shareholder. It will, therefore, be a question of fact and a matter of inference in each case whether any "relatives" forming themselves into a company acted as a group or block in concert in controlling the affairs of the company. Relationship would not, per se, lead to such a conclusion.

The Tribunal in its order observed :

> "Sir A. K. Jain became major on March 5, 1952. Therefore, as at the end of the two previous year, his holding of 10,000 shares cannot ipso facto be amalgamated with the shareholding of Sri S. P. Jain as if he was the nominee of his father. The shareholding of 10,000 share by Mrs. Rama Jain has also to be left out of account since, as already observed, there is no finding that Sri S. P. Jain provided the consideration for the acquisition of 10,000 shares held by her. Assuming, therefore, that Sri S. P. Jain was the controlling shareholder, the shares held by the members of the 'public' which would include Sri A. K. Jain and Mrs. Rama Jain would be at least 22,000 shares."

In the supplementary statement of case filed by the Tribunal enclosing various orders and other documents, it is shown that S. P. Jain was director of the company from August 3, 1950, to September 25, 1950. He was appointed managing director from June 6, 1953, subject to approval of the Government. A. K. Jain was director of the company from August 3, 1950, even when he was a minor (his date of birth being March 5, 1934) and was appointed deputy managing director from June 6, 1953, subject to approval of the Government. R. Sharma was director from August 3, employee of Sahu Jain Limited. N. C. Jain was director from September 25, 1950, to March 25,

1954. He was secretary of S. P. Jain and employee of Ashoka Agencies Limited.

From the above it appears that the deputy managing director and the two other directors held amongst themselves 10,020 shares and out of the balance 30,000 shares were held by the relations of the managing director, namely, by the father, the mother and the minor brother. It also appears that S. P. Jain along with Ashok Kumar Jain, R. Sharma and N. C. Jain were the promoters and subscribed to the memorandum of association at the start of the company in July, 1950. It also appears Ashok Kumar Jain, director, was getting a remuneration of Rs. 6,000 per month with effect from September, 1951, in accordance with the resolution passed in an extraordinary general meeting of the shareholders on October 1, 1951. At the meeting of the board of directors of the company, were authorised to execute managing agency agreements with different companies. Ashok Kumar Jain was generally presiding over the meetings from November, 1950.

The Tribunal further observed in its statement of case that :

> "A perusal of the minutes of the proceedings of the general meetings does not lead to any inference that Sri S. P. Jain, Smt. Rama Jain and Sri A. K. Jain were necessarily acting in concert. On the other hand, it appears that, despite his young age, Sri A. K. Jain seems to have been taking active interest in the management of the affairs of the assessee-company and the companies managed by it. Unless it is to be presumed that because of the relationship, Sri S. P. Jain, Smt. Rama Jain and Sri A. K. Jain should be regarded as acting in concert, there is no other material on record on the basis of which such a conclusion could be supported."

The Tribunal also observed :

> "that in spite of the opportunity afforded by the Appellate Assistant Commissioner, the Income-tax Officer had not brought on record materials to show that the voting rights of Mrs. Rama Jain or Sri A. K. Jain were controlled by Sri S. P. Jain."
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> The Tribunal concluded by observing that "the revenue had failed to establish that Sri S. P. Jain, his wife and his son, Sri A. K. Jain, were acting in concert".

Section 23A again came up for consideration before this court in Commissioner of Income-tax v. East Cost Commercial Co. Ltd. This court made a reference to the Raghuvanshi Mills' case where it was observed :

> "The word "public" is used (in the Explanation) in contradistinction to one or more persons who act in unison and among whom the voting power constitutes a block. If such a block exists and possesses more than seventy-five per cent. of the voting power, then the company cannot be said to be one in which the public are substantially interested..... the test is first to find out whether there is an individual or group which controls the voting power as a block. If there be such a block, the shares held by it cannot be said to be "unconditionally" and "beneficially" held by members of the public'."

This court further observed :

> "The Tribunal had to decide in the first instance whether there was a group of persons acting in concert holding a sufficient number of shares which may control

> the voting as a block. But the existence of a block is not decisive. If there be a group of persons holding control over voting the company would still be a company in which the public are substantially interested, if twenty-five per cent. or more of the voting power has been allotted unconditionally to and beneficially held by the public and the shares were in the previous year subject of dealings in any stock exchange in the taxable territories or were in fact freely transferable by the holders to other members of the public. The two enquiries are distinct."

This court further referred to Jubilee Mills' case and Raghuvanshi Mills' (SC)) and observed as follows :

> "But in Commissioner of Income-tax v. Jubilee Mills Ltd., this court held that no direct evidence of over act or concert between the members of the group having control over voting was necessary to prove that the company was not one in which the public were substantially interested. It was observed in Raghuvanshi Mills' case that 'in deciding if there is such a controlling interest, there is no formula applicable to all cases. Relationship and position and director are not by themselves decisive. If relatives act, not freely, but with others, they cannot be said to belong to that body, which is described as "public" in the Explanation'. In Jubilee Mills' case, this court elaborated those observations and stated :
>
> The test is not whether they have actually acted in concert but whether the circumstances are such that human experience tells us that it can safely be taken that they must be acting together. It is not necessary to state the kind of evidence that will prove such concerted actings. Each case must necessarily be decided on its own facts'."

This court finally in the above East Coast Commercial Co. 's case concluded as follows :

> "On an analysis of the reasons recorded by the Tribunal and the High Court, it is clear that the Tribunal held that the Kedias did not form a controlling group because there was no evidence that they actually controlled the voting, even though they held more than seventy-five per cent. of the shares issued by the company : the High Court observed that the members of the Kedia family held 4,015 shares of the company and were in a position to control the affairs of the company, but there was no evidence to show that they did in fact act in concert and controlled the affairs of the company as a block. But, as already observed, if the members of the Kedia family formed a block and held more than seventy-five per cent. of the voting power, it was not necessary to prove that they actually exercised controlling interest. It is the holding in the aggregate of a majority of the shares issued by a person or persons acting in concert in relation to the affairs of the company which establishes the existence of a block. It is sufficient, if having regard to their relation, etc., their conduct, and their common interest, that it may be inferred that they must be acting together; evidence of actual concerted acting is normally difficult to obtain, and is not insisted upon."

We may also observe in passing that it does not appear that the East Coast Commercial Co.'s case) was referred to during the hearing in, nor was it noticed by, the High Court.

The Tribunal in the supplementary statement observed as follows :

> "Unless it is to be presumed that because of relationship, Sri S. P. Jain, Smt. Rama Jain and Sri A. K. Jain should be regarded as acting in concert there is no other material on record on the basis of which such a conclusion could be supported."

The High Court also observed to the same effect :

> "It may be that in view of the relationship of the parties as to a group consisting of the father, two minor sons and their mother, a possible inference was that the relationship was such that they could reasonably be taken to be acting as a group in concert..... "but" the assessee could not be placed in the category of such a company merely because of the close relationship."

Keeping in the forefront the test laid down by this court in East Coast Commercial Co.'s case Mr. Sen, on behalf of the revenue, submitted for our consideration the following fact and circumstances from which, according to counsel, an inference can be reasonably drawn about the controlling power in a block confined to a family group holding more than 75 per cent. shares :

> (1) 80 per cent. of the share capital (40,000 out of 50,000) is held by S. P. Jain, his wife and two sons, one of whom was a minor throughout the period of the two accounting year and the other son, A. K. Jain, for a portion of the period up to March, 1952. The remaining 20 per cent. of the shares was held by the companies which were under the control of S. P. Jain and out of which 20 shares were held by two employees under the control of S. P. Jain.
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> (2) A. K. Jain was appointed as director in the company in August, 1950, when he was a minor, aged 16 years, and he become the managing director on February 1, 1954, at a salary of Rs. 6,000 per month. According to counsel this could not have been possible if he was not the son of the controlling shareholder, S. P. Jain.
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> (3) S. P. Jain, who was a director, resigned making room for his private secretary, N. C. Jain, for appointment as director.
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> (4) During the assessment year 1953-54, the assessee-company claimed Rs. 2,02,500 as loss in a transaction in hessian through Messrs. Kabra & Co. in settlement of August 18, 1952, and the same amount was shown as profit in hessian through the same broker by Smt. Rama Jain, wife of S. P. Jain, in the settlement.
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> (5) S. P. Jain, A. K. Jain, R. Sharma and N. C. Jain were the promoters of the company and were the signatories to the memorandum of association.

Mr. Hardy, the learned counsel for the respondent, on the other hand, replied to the submissions as follows :

> (1) Rama Jain and A. K. Jain are independent assessees. The minutes of the board's meetings clearly show A. K. Jain as a competent director taking independent decisions. Mere relationship, therefore, would not lead to the conclusion that these two shareholders acted with control the voting power of the minor son, Alok Prakash Jain, as his natural guardian. According to Mr. Hardy, if Rama Jain and A. K. Jain

are holding 20,000 shares out of 50,000, they cannot be held to be acting in concert with S. P. Jain and section 23A will not be attracted.

(2) With regard to the second submission of Mr. Sen, Mr. Hardy submits that there is sufficient evidence in the record, which is even referred to in the further statement of the case, that A. K. Jain was an independent shareholder and was not under the control of S. P. Jain or any other director or shareholder. He further submits that there is no evidence whatsoever that the money for purchasing the shares of A. K. Jain or even of Rama Jain was advanced By S. P. Jain.

(3) With regard to the third submission of Mr. Sen, Mr. Hardy had to admit that N. C. Jain was director from 1950 to 1954 and S. P. Jain was director from August 3, 1950, to September 25, 1950, and S. P. Jain became the managing director of the company on June 6, 1953, subject to the approval of the Government on a remuneration of Rs. 8,000 per month and A. K. Jain was appointed as deputy managing director on a remuneration of Rs. 6,000 per month subject to the approval of the Central Government (vide minutes of the board's meeting of June 6, 1953). According to Mr. Hardy, appointment of directors or even managing director is a regular matter of the company and no particular significance should be attached to these appointments.

(4) With regard to the fourth submission Mr. Hardy submits that such transactions are common with brokers and even the purchaser is not known in most of the cases. Hence, no undue should be attached to the hessian transaction so as to influence the conclusion. It is also pointed out that there was no controversy about the genuineness of the hessian transaction.

We are of the view that the genuineness of the aforesaid transaction is, however, irrelevant for the purpose of considering its effect in acting in concert by the shareholders.

(5) With regard to the fifth submission Mr. Hardy submits that it is true that S. P. Jain, R. Sharma and N. C. Jain were the promoters of the company but admittedly two of them, namely, R. Sharma and N. C. Jain, were outsiders. That they were employees would not affect their character as shareholders of the company or even as directors.

It is clear that this company was a family concern with only 20 shares out of 50,000 shares allotted to two outsiders who again happened to be paid employees. The presence of these two outsiders is of the least significance in the matter of management of the affairs of the company. It is true that most of the meetings of the board of directors were presided over by A. K. Jain with either of the two employees or one of them attending the same. It must, however, be noted that A. K. Jain became a director even when he was a minor aged 16 years. He would not ordinarily be able to play the role he is supposed to have done in the board's meetings unless S. P. Jain was confident that the board war carrying out his mandates with regard to the affairs of the company. It is also true that A. K. Jain and the other directors were authorised to sign agreements on behalf of the company, but this is not of great significance since this was in pursuance of a decision of the board's meeting which could not have been passed but for the concurrence of S. P. Jain. There is no evidence whatsoever to show that Rama Jain, wife of S. P. Jain, was at all independently acting.

When a company is composed mostly of family members owning a lion's reach of section 23A(1)

will be on the shareholders by adducing some positive evidence about the absence of control by the controlling shareholders.

So far as Rama Jain is concerned it is not possible to hold that S. P. Jain would be able to control his wife's voting power along with that of his minor son, Alok Prakash Jain. It is true that mere relationship or being a director is not decisive. As a matter of fact no single factor can be decisive but having regard to the totality of the circumstances revealed in the case and the conduct of the transactions of the company taken with the relationship, which in the circumstances of the case is not a negligible element, we are clearly of the opinion that it is a case in which it cannot be said that the "public" is substantially interested in 25 per cent. or more shares of the company. Even if we allow A. K. Jain to be a member of the "public", he only holds 10,000 shares and taken with 2,000 shares of Ashoka Agencies Ltd., the total shareholding comes only to 12,000 shares, that is to say, 500 less than the minimum shareholding requisite to earn the benefit of the third proviso to section 23A read with the Explanation.

Further, between August 11, 1951, and May 1, 1952, A. K. Jain and two employee-directors, the later having a modicum of 10 shares each, apparently took all decisions for the company in the board's meetings. This is not ordinarily possible but for collaboration with the major shareholders. This is a case where more is meant then meets the eye. We are unable to hold in this case, in the absence of any reliable evidence to the contrary, that the voting power of the three directors was free and uninhibited and not within the orbit of control of the other major shareholders, S. P. Jain and Rama Jain, acting in concert. It is a clear case of all the shareholders acting in concert and in unison and the two employee-directors were merely dummies. There is not the slightest inkling of "public" being interested, far less substantially interested, in this company, There was no one who could come within the term "public" outside the ring of the shareholders acting in concert for concert for their own ends with a common purpose. There is no evidence whatsoever in this case that the shareholders did not cohere together in the matter of transaction of the company's affairs. When the reality is manifest some reliable evidence within the special knowledge of the assessee must be forthcoming from its side to contradict the obvious in order to be covered by the exception. This has not happened in this case.

Unless the two employees were the nominees of the major shareholders it is ordinarily absurd to suppose that they could aspire to be and become directors of the company. The Appellate Assistant Commissioner in his order, which is annexed with the statement of the case, mentions that :

> "In fact Sri S. P. Jain as a controlling shareholder had brought himself in as a director of the company right from the inception of the company and was the first director of the company from 3-8-50 to 26-9-50. From September, '50 to March, '54, however, he temporarily gave up the directorship by putting in an employee as a nominee-director, Sri N. C. Jain, for the intervening period so that there may be no hitch in the appellant-company being appointed as managing agent of certain other companies under his control on which also Sri S. P. Jain was a director, such as the Rohtas Industries Ltd., and New Central Jute Mills Ltd. As soon as this objective was achieved, Sri S. P. Jain again staged a come-back as a director of the appellant-company on 25-3-54, when the nominee-director, Sri N. C. Jain, resigned his directorship to make room for his master, Sri S. P. Jain."

The factual position, not the opinion, revealed in the above extract is more than eloquent with regard to the core of the company.

Having regard to the intimate relationship of the shareholders, with not the least evidence of any disconcert amongst them the ordinary expectation for individual profit in commercial undertakings, natural reluctance to forgo the same, the history of the company and its continued smooth working in a manner which is normally inconsistent with anything other than full unison amongst the shareholders in decisions about the conduct of the company's affairs in common interest of all, this was a company of one paramount mind operating without the least doubt. The board's meetings are evidence of a well- organised. well-knit, close unity of views in all affairs and which in the ordinary course of human conduct would not have been at all possible but for a single or concerted action in the company's management by a controlling group. When all the above conditions are present in a company, the onus would be on the assessee to satisfy by some reliable evidence that what appears on the surface is that which is real. That is not to say that the revenue has no burden to bring the case within the mischief of section 23A.

Application of law cannot be bereft of common sense. The object of section 23A being to prevent avoidance of super-tax by the shareholders by piling up the profits of the company in its own hands, the facts and circumstances revealed in this case clearly bring the company within the reach of that section. We are unable to accede to the submission of Mr. Hardy in this case that, because A. K. Jain and Rama Jain were independent assessees and A. K. Jain was presiding in the board's meetings and as such was taking independent decisions and was also doing extra work for the company in Calcutta on salary basis, they should be held to be members of the "public" who were substantially interested in the company with the requisite shareholding for the purpose of the Explanation read with the third proviso.

The High Court was, therefore, not right in answering the question in favour of the assessee and against the revenue. We, therefore, answer the original question in the negative and the revised question in the affirmative both in favour of the revenue. The appeals are allowed but we leave the parties to pay and bear their respective costs.

Appeals allowed.

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