SUPREME COURT OF INDIA

North Bengal Sugar Mills Co. Pvt. Ltd.

Vs.

Commissioner of Income Tax, Calcutta

(B J Reddy and B Kirpal JJ.)

08.11.1995

ORDER

1. This appeal arises from the judgment of the Calcutta High Court answering the question referred to it in the affirmative, i.e., in favour of the Revenue. The question referred under Section 66(1) of the Indian Income Tax Act, 1922 was

"whether on the facts and in the circumstances of the case, the provisions of Section 23-A could be applied to the assessee for the Assessment Year 1960-61".

2. The assessment year concerned herein is 1960-61, the accounting year whereof is the year ending on 31-8-1959. The assessee owns a sugar mill and a farm attached to it in what was then East Pakistan. At the relevant time there were restrictions upon remittances from Pakistan to India. The books of the assessee for the said year showed a profit of Rs 93,449, after making provision for taxation in India and Pakistan. The Income Tax Officer, however, made an assessment on an income of Rs 6,92,441. After deducting the tax payable thereon he arrived at the balance of Rs 3,80,842.55. He found that the assessee had not declared the dividends within twelve months of the expiry of the accounting year. Accordingly, he levied additional super tax on the undistributed balance of Rs 3,80,842.55 under Section 23-A. The assessee's contention was that it had declared the dividend of Rs 1,80,000 within forty-six days of the expiry of the aforesaid twelve months' period and that this delay had occurred on account of the fact that the account books could not be brought to India and that a local auditor had to be appointed, all of which took some time. It submitted further that since the declaration and payment of dividends was conditional upon the Government of Pakistan allowing remittance facilities, and as the remittance was not possible, the dividends were not declared. The Income Tax Officer was not satisfied with the said reasons and levied the additional super tax, as stated above.

3. An appeal preferred by the assessee to the Assistant Appellate Commissioner was dismissed. The assessee carried the matter to the Tribunal. The Tribunal accepted the reasons put forward by the assessee for not declaring the dividends within the aforesaid twelve months' period. It opined that the provisions contained in Section 207 of the Companies Act, 1956 or for that matter the provisions contained in the proviso to Section 45 of the Income Tax Act were not reasons enough for rejecting the assessee's case. The Tribunal also found that the assessee had incurred substantial

liabilities in India in excess of the advances made by it and that the assessee could not have declared the dividends out of its Indian resources. Accordingly, it cancelled the order of the Income Tax Officer made under Section 23-A of the Income Tax Act. Thereupon, the Revenue asked for and obtained the aforesaid reference.

4. When the reference came up for hearing before the High Court, it appears that no one appeared for the assessee. The High Court heard the learned counsel for the Revenue and after referring to Section 45 of the Income Tax Act and Section 207 of the Companies Act, 1956, held that the reasons assigned by the assessee for not declaring the dividends within the prescribed period were not acceptable and that action was rightly taken against it under Section 23-A. The correctness of the said view is questioned in this appeal.

5. Sub-section (1) of Section 23-A, as it obtained at the relevant time, read thus:

"23-A. Power to assess companies to super tax on undistributed income in certain cases.--(1) Where the Income Tax Officer is satisfied that in respect of any previous year the profits and gains distributed as dividends by any company within the twelve months immediately following the expiry of that previous year are less than the statutory percentage of the total income of the company of that previous year as reduced by-

(a) the amount of income tax and super tax payable by the company in respect of its total income, but excluding the amount of any super tax payable under this section;

(b) the amount of any other tax levied under any law for the time being in force on the company by the Government or by a local authority in excess of the amount, if any, which has been allowed in computing the total income; and

(c) in the case of a banking company, the amount actually transferred to a reserve fund under Section 17 of the Banking Companies Act, 1949;

the Income Tax Officer shall, unless he is satisfied-

(i) that, having regard to the losses incurred by the company in earlier years or to the smallness of the profits made in the previous years, the payment of a dividend or a larger dividend than that declared would be unreasonable; or

(ii)that the payment of a dividend or a large dividend than that declared would not have resulted in a benefit to the Revenue;

make an order in writing that the company shall, apart from the sum determined as payable by it on the basis of the assessment under Section 23, be liable to pay super tax at the rate of fifty per cent, in the case of a company whose business consists wholly or mainly in the dealing in or holding of investments, and at the rate of thirty-seven per cent, in the case of any other company on the undistributed balance of the total income of the previous year, that is to say, on the total income as reduced by the amounts, if any, referred to in Clause (a), Clause (b) or Clause (c) and the dividends actually distributed, if any."

The object of this section as stated by this Court in CIT v. Abdul Rahim Osman and Co. (India) (P)

Ltd., is:

"3. This provision is procedural and applies only to companies in which the public are not substantially interested. It seems to have been enacted with a view to deter private companies which do not distribute more than 60% of their assessable income on pain of exposing them to the drastic consequences of subjecting their undistributed balance of the net income to additional super tax. The object of the section is to prevent the shareholders from adopting a device to avoid payment of super tax, inasmuch as the rates of super tax for the companies being lower, there may be a temptation to get the company to accumulate profits and capitalise them, such as for instance to issue bonus shares which were not assessable as income in the hands of the shareholders. It is to avoid these artifices and force such companies to declare the minimum statutory dividends, though in the light of the changed definition of 'dividend' under Section 2(6-A) profits may attract tax even when they reach the shareholder in capitalised forms, or where they are distributed to them on liquidation from accumulated profits over the years, they will be chargeable as dividends. In cases where the provisions have not been complied with, the Income Tax Officer, with the previous approval and consent of the Inspecting Assistant Commissioner, will get jurisdiction to make an order if at the time of the passing of the order it is found that the company has not distributed by way of dividends within twelve months immediately following the accounting year less than the statutory percentage of its total income of the accounting year as reduced by the amount of taxes payable by the company and in the case of banking companies the amount actually carried to a reserve fund under a statutory compulsion."

It may also be noticed that the provision contained in Section 23-A is stringent in nature and may have to be construed strictly.

6. The main question in this matter is whether the reasons assigned by the appellant are relevant in law and adequate in the circumstances of the case. On this aspect, it is relevant to notice the decision of this Court in CIT v. Gangadhar Banerjee and Co. (P) Ltd., holding that Clauses (i) and (ii) of Sub-section (1) of Section 23-A were not exhaustive and that the Income Tax Officer has to and is entitled to look to all the relevant circumstances to determine whether the non-declaration of dividends was justified. For this purpose, it has been held, the Income Tax Officer has to place himself in the position of the Board of Directors and examine the said question. This is what the Court said:

"The argument mainly centerd on this part of the section. Would the satisfaction of the Income Tax Officer depend only on the two circumstances, namely, losses and smallness of profit? Can he take into consideration other relevant circumstances? What does the expression 'profit' mean? Does it mean only the assessable income or does it mean commercial or accounting profits? If the scope of the section is properly appreciated the answer to the said question would be apparent. The Income Tax Officer, acting under this section, is not assessing any income to tax: that will be assessed in the hands of the shareholder. He only does what the directors should have done. He puts himself in the place of the directOrs. Though the object of the section is to prevent evasion of tax, the provision must be worked not from the standpoint of the tax collector but from that of a businessman. The yardstick is that of a prudent businessman. The reasonableness or the unreasonableness of the amount distributed as dividends is judged by business considerations, such as the previous losses, the present profits, the availability of surplus money and the reasonable requirements of the future and similar others. He must take an overall picture of the financial position of the business. It is neither possible nor advisable to lay down any decisive tests for the guidance of the Income Tax

Officer. It depends upon the facts of each case. The only guidance is his capacity to put himself in the position of a prudent businessman or the director of a company and his sympathetic and objective approach to the difficult problem that arises in each case. We find it difficult to accept the argument that the Income Tax Officer cannot take into consideration any circumstances other than losses and smallness of profits. This argument ignores the expression 'having regard to' that precedes the said words."

This decision has been followed later in CIT v. Asiatic Textiles Ltd., .

7. Looking at the matter from the above point of view, can it be said that the reasons assigned by the assessee, the factual correctness whereof has not been disputed by the Revenue, were not adequate for not declaring the dividends within the prescribed period of twelve months. We think not. Admittedly the money had not been received in India within the said period. Even the books of account could not be brought from Pakistan. The assessee was obliged to appoint a local auditor. There were substantial liabilities which the assessee had incurred in India. Its Indian income was not sufficient to declare dividends. Could it be said in these circumstances that not declaring the dividends within the prescribed period of twelve months was unreasonable and was intended to defeat the object underlying Section 23-A? We are of the opinion that it cannot be so said. The Tribunal was, therefore, justified in accepting the explanation put forward by the assessee. It appears that because the assessee was not represented before the High Court, the above facts could not be brought to the notice of the High Court and a decision adverse to the assessee was rendered.

8. For the above reasons the appeal is allowed, the judgment of the High Court is set aside and the question referred to the High Court is answered in the negative, i.e., in favour of the assessee and against the Revenue. No costs.