

# CALCUTTA HIGH COURT

General Family Pension Fund

Vs

Commissioner of Income-Tax

(Gentle, J.)

12.04.1946

## JUDGMENT

### **Gentle, J.**

1. The General Family Pension Fund was incorporated under the Indian Companies Act, 1882 on 17th August, 1906; it is a company limited by guarantee; it has no share capital and its members are confined to persons who are subscribers for grants of pensions and annuities and who hold entrance certificates; the liability of each member is limited to a nominal sum of Rs. 5; since it complied with the provisions of Section 26 of the above Act, a licence was granted by the Bengal Government permitting the company to be registered without the word "limited" being included in its name.

The objects of the company, as contained in its Memorandum of Association, inter alia, are :-

3. (a) To acquire and take over as a going concern and to carry on and conduct and continue the objects of an existing unincorporated association or institution called the General Family Pension Fund founded and formed for the purpose of carrying on any business that has for its objects the acquisition of gain within the meaning of Section 4 of the said Act (Indian Companies Act, 1882).

(b) To grant terminable pensions or annuities dependent on human life or any other event or contingency in favour of any subscriber and/or any nominee or nominees (within the categories therein mentioned) of a subscriber to the funds of the company.

(d) To grant invest and deal with the moneys of the company not immediately required.

(g) To pay out of any of the companys funds all expenses of management of the companys business and objects.

4. The income and property of the company whensoever derived shall be applied solely towards the promotion of the business and objects of the company as set forth in the Memorandum of Association and no portion thereof shall be paid or transferred directly by way of dividend or bonus or otherwise by way of profit to the members of the company. Provided that nothing therein contained shall prevent (i) payment of specified salaries and wages and (ii).....granting to any member a pension or annuity.

It is conceded by the Commissioner of Income-tax that the company carried on the business of a life assurance company. The Indian Life Assurance Companies Act, 1912, applies to all persons or bodies of persons, whether corporate or incorporate, (therein referred to as life assurance companies), who carry on such business within British India except, inter alia, to any fund which the Governor-General in Council may, by notification exempt from the operation of the Act. By Notification No. 7345-97 dated 13th September, 1913, the General Family Pension Fund was exempted from the operation of that Act. It is also conceded by the Commissioner that the transactions between the company and its members are mutual dealings and that income-tax is not assessable upon the surplus of the members subscriptions; this concession was made in pursuance of the decision in *New York Life Insurance Company v. Styles*, the principles of which, it is admitted, apply in India. It is convenient hereafter to refer to the General Family Pension Funds as the Fund.

This reference is concerned with the assessments for the years 1937-38 and 1938-39. Since they are in respect of years prior to the passing of the Indian Income-tax (Amendment) Act, 1939, the provisions of the Indian Income-tax Act, 1922 (hereinafter called the Act), as enacted before the Amendment Act of 1939, will apply to this reference.

The questions referred for the opinion of this Court are :-

1. Whether the decisions of the Assistant Commissioner of Income-tax, Calcutta, for the years 1928-29 to 1935-36 are binding upon the Income-tax Officer upon the principles of *res judicata* or otherwise ?
2. Whether the income, profits and gains of the General Family Pension Fund for the year ending the 31st December, 1936, should be assessed under rule 25 of the Indian Income-tax Rules in the form then in force ?
3. If the answer to (2) is in the affirmative, whether in applying the said rule 25, from the surplus so ascertained, the Fund is at liberty to appropriate its non-mutual receipts, that is income from its investments, in the first instance, against its expenditure and to charge any balance of expenditure against its mutual receipts, that is income from members subscriptions, thus leaving

a final balance of mutual receipts which are non-taxable under the authority of Styles case ?

The Fund has considerable sums invested in Indian Government and similar securities and also some other investments, e.g., banking, Indian Treasuries and sterling securities brought into British India. The assessment for the year 1937-38 was made with regard to the Funds financial year ending on 31st December, 1936, and the other assessment relates to the next financial year. Reference, in any detail to the earlier year is alone necessary as the later year, except for some variations in amounts, is substantially the same. During 1936 the total investments amounted in value to Rs. 77 lakhs, approximately, of which the main portion was Indian Government and like securities; the investment income amounted to about Rs. 4,75,000 in respect of which in most instances, income-tax was deducted at source; the other receipts to use a neutral term, were from the members and amounted to a sum slightly in excess of Rs. 1 lakh, being their annual subscriptions for pensions and annuities; the Fund paid about Rs. 4,12,000 in pensions and annuities and about Rs. 66,000 for management expenses.

For many years, the profits of the Fund have been ascertained by means of quinquennial actuarial valuations. In the valuation for the quinquennium ending on 31st December, 1934, the estimated surplus was Rs. 4,23,681 which sum was the basis for ascertainment of the profits during the five years. During a considerable number of years, up to and including the first assessment for the year 1937-38, assessments for income-tax were based upon the average annual net profits disclosed by the last preceding quinquennial actuarial valuation with, possibly, some additions to which reference is unnecessary. In respect of the year 1937-38, the Income-tax Officer first made an assessment based upon the actuarial valuation; subsequently he served a notice upon the Fund under Section 34 of the Act, re-opened the assessment and re-assessed the Fund upon its income during the financial year ending 31st December, 1936, from Government securities (under Section 8) and from the other investments (under Section 12) allowing deductions only of bankers charges or commission (under section 8) and a proportionate amount of management expenses commensurate with the amount of the other investment income to the total amount of the gross receipts, comprising subscriptions from members, interest upon Government securities and upon other investments. In the first assessment for the year 1937-38 the profits were assessed as nil and a sum of about Rs. 70,000, representing income-tax deducted at source in respect of interest upon investments, was repayable. By the second assessment Rs. 97,000 income-tax was due, which amount included the sum of about Rs. 70,000 above-mentioned, which had been refunded. The receipts from members were not included in this assessment and the only amount allowed for management expenses was Rs. 2,526 out of Rs. 66,000. Substantially, the difference between the two assessments is that the Fund was required, by the second assessment to pay Rs. 27,000, in addition to tax upon the interest from investments, instead of being entitled according to the first assessment, to refund of Rs. 70,000. The assessment for the year 1938-39 was made

by the same method as the second assessment for the previous year and by which the sum of Rs. 24,609 tax became payable, in addition to tax deducted at source in respect of the investment income. Prior to the second assessment for the year 1937-38 it would seem that the whole of the Funds receipts were considered to appertain to its business of a mutual insurance company and that rule 25 of the Income-tax Rules, which was then in force, was applicable to the Fund. This rule provides that :

"In the case of Life Assurance Companies incorporated in British India whose profits are periodically ascertained by actuarial valuation, the income, profits and gains of the Life Assurance Business shall be the average annual net profits disclosed by the last preceding valuation, provided that any deductions made from the gross income in arriving at the actuarial valuation which are not admissible for the purpose of income-tax assessment, and any Indian income-tax deducted from or paid on income derived from investments before such income is received, shall be added to the net profits disclosed by the valuation."

After the first assessment for 1937-38 had been made by application of rule 25, the Income-tax department subsequently formed the opinion that the rule did not apply to the company and it should be assessed upon its actual income during the year preceding the year of assessment, namely, in respect of its financial year ending on 31st December, 1936. Since the income for that year had not been the subject of the first assessment, the view taken was that that income had not been assessed but had escaped assessment, and the provisions of Section 34 were attracted; notice was given under the section, and the second assessment was made. The correctness of the departments opinion and the validity of the second assessment is dependent upon the question whether rule 25 is applicable to the Fund. Further, the validity of the assessment for 1938-39 will also be dependent upon the same question; this assessment was made in respect of the financial year ending on 31st December, 1937.

Dr. Gupta, for the Commissioner of Income-tax, contended that an assessment upon a previous years income is correct and that rule 25 is in applicable to the Fund, upon the following grounds :-

1. The rule does not apply to a life assurance company which is exempted from the provisions of the Life Assurance Companies Act.
2. The rule does not apply to a mutual life assurance company since it does not make and is precluded from making profits upon its life assurance business.
3. The rule is not the sole method of computation of the income or profits of a life assurance company, and the provisions of Sections 8, 10 and 12 of the Act are not abrogated nor excluded

by the rule.

4. Assuming the rule applies to a mutual life assurance company, the income or profits to be ascertained by its operation are those which are solely and directly derived from its life assurance business and not those derived from its securities or investments which are not an integral part of the business of a life assurance company.

5. Since the principles in Styles case apply to the Fund, by which receipts from its subscribers in respect of life assurance are not subject to assessment to income-tax, rule 25 has no application to the Fund.

After the Indian Income-tax (Amendment) Act, 1939 was passed rule 25 ceased to be in force, and the profits and gains of life assurance business are now ascertained by application of the rules contained in the Schedule to the Act of 1922, added to it by the Amending Act; rule 9 of the rules in the schedule expressly provides that those rules apply to a mutual insurance company. Dr. Gupta argued that, since the new rules are expressly made liable to a mutual company, upon which rule 25 is silent it should be inferred that the rule was inapplicable to mutual company. The provisions of a subsequent enactment are not a safe guide to ascertain the meaning and effect of a repealed earlier enactment dealing with the same subject matter. Although an earlier enactment may not expressly make its provisions applicable in a particular instance, it does not necessarily follow that the provisions do not apply because a later enactment dealing with the same subject matter, contains an express provisions for applicability in that instance. To ascertain its effect, the earlier enactment must be construed by reference to its provisions and those of the statute in which it is contained and not by reference to the later enactment.

The exemption from the operation of the Indian Life Assurance Companies Act, it is argued prevents the application of rule 25. The rule does not restrict its application to those companies which are subject to that Act nor make it inapplicable to companies which are exempted from the operation of the Act. If limited application was intended, language to that effect could have been used, but there is none. The non-applicability of the Act does not change the nature of the Funds business, which is that of life assurance. In its terms the rule applies to all Indian life assurance companies and the exemption of the Fund from the operation of the Act does not prevent application of the rule to it.

The argument supporting the assessments is put in this way. Since the Fund is a mutual assurance company, it does not derive income or make profits out of insurance transactions with its members and receipts from those transactions and the income from investments cannot be ascertained by application of rule 25; the income from Government securities has to be assessed

under Section 8, which permits only a deduction in respect of bankers commission upon realisation, no other allowance, e.g., management expenses, can be made; hence, in the assessments under Section 8, only bankers commission is deducted, and no allowance is made of any part of the management expenditure; the remaining income, by way of interest from the Funds other investments, falls within Section 12, which permits a deduction being made of expenditure solely incurred to obtain that income, and an allowance is made of a proportionate amount of the management expenses ascertained by computing the amount which the income received under this head bears to the total income; the income from investments is not income, profits or gains of the Funds business of insurance and therefore does not fall within Section 10 since it is not part of that business.

The assessments exclude the premium income, or subscriptions from the members. Substantially, the whole expenses of management are treated as attributable to the transactions with the members; the position adopted is that because of the non-assessability of the receipts from that source, no deduction for management expenses can be made, save for a small sum with respect to the investment income assessed under Section 12; in the assessment for the year 1937-38 a sum of Rs. 2,526 out of a total management expenses of Rs. 66,036 and for the year 1937-38 a sum of Rs. 117 out of Rs. 69,781 have been allowed under that section.

The effect of rule 25 is that the income, profits and gains of a life insurance company shall be the average annual net profits disclosed by a periodical actuarial valuation when such company ascertains its profits by that method. The contention by the Commissioner is that the Fund must derive "profits" from its life assurance business as a condition precedent to the applications of the provisions of the rule; if there are no "profits" from that business, the rule cannot be applied; the Fund is a mutual insurance company and the receipts from its members are mutual dealings, the excess of those receipts over expenditure is not "profits"; and since there are no profits, the condition precedent is not fulfilled and the rule is inapplicable.

Styles case is relied upon as having decided that the receipts, or the excess of receipts over expenditure from members of a mutual life assurance company, are not income or profits. The question for decision in that case was whether income-tax was payable upon the surplus from those receipts, after discharging the expenses for which they were obtained from members. This is made clear by the opening words of the argument for the insurance company at page 387 of the report. In *Commissioners of Inland Revenue v. Cornish Mutual Assurance Co., Ltd.*, Pollock, M.R., at p. 852 and Warrington, L.J., at page 857 pointed out in the Court of Appeal that, in Styles case the House of Lords was not called upon to decide whether the assurance company was trading with its members or whether the surplus was profits but whether the surplus was profits or gains within the meaning of the English Income Tax Act. At page 866, of the report in

the House of Lords, Viscount Cave, L.C., said : "The point to be decided by the House in that case (Styles) was whether the company there concerned was carrying on a trade from which it derived profits which were subject to tax and the the actual decision was there were no such profits." Lord Bramwell, at page 394 in Styles case said : "The appellants do not carry on a profession, trade, employment or vocation from which profits or gains arise or accrue within the meaning of the Income-tax." The contention by the Commissioner of Income-tax, in the present reference, depends mainly upon the observations of Lord Watson, at page 394 in Styles case, that "when a number of individuals agree to contribute funds for a common purpose, such as the payment of annuities or of capital sums, to some or all of them, on the occurrence of events certain or uncertain and stipulate that their contributions, so far as not required for that purpose, shall be repaid to them, I cannot conceive why they should be regarded as traders, or why contributions returned to them should be regarded as profits." With respect to these observations Pollock, M.R., said, in the Court of Appeal, in Cornishs case at page 853 : "It is quite true that Lord association were or were not trading". The Master of the Rolls then cited part of the observations by Lord Watson which I have quoted, and continued : "It is said that we ought to take note that those two noble Lords expressed the opinion that a mutual association, a body of persons associated together for the purpose of mutual insurance, do not carry on a trade, but it is to be observed that that is not the basis of the decision and both those nobles Lords, when they are dealing with the question of trading, refer to it incidentally in order to arrive at whether or not the profits or gains, which are the result of that, are subject to income-tax. They do not refer to the question of trading per se and alone, but only to the question of trading incidental to the question which they had to decide, namely whether the surplus was subject to income-tax." With respect to Lord Watsons observations Viscount Cave said, at page 867 of the report in the House of Lords in Cornishs case, that "I cannot help thinking that the very learned Lord directed his observations only to the real question before the House, namely, whether there were taxable profits within the Income-tax Acts."

Two earlier decisions, by the Court of Appeal, were not cited to, and were not considered by, the House of Lords in Styles case but they were quoted with approval by Pollock, M.R., in the Court of Appeal and by Lord Cave in the House of Lords, in Cornishs case. Arthur Average Association for British and Colonial Ships and Padstow Total Loss and Collision Assurance Association concerned mutual marine assurance associations, in which the opinions were expressed that each such association carried on the business of marine insurance and carried it on for the purpose of gain for itself or for its individual members. In Cornishs case, Viscount Cave referred to the Arthur Average and Padstow cases as supporting the view, which he expressed, that whilst a mutual assurance company only carries on business with its members, yet as every person who chose to effect a policy with the company ispo facto became a member, the restriction did not appear to prevent the transactions of the company from being business

transactions. In Cornish's case it was held that a mutual assurance company carried on business and was assessable to Corporation Profits Tax imposed by the English Finance Act, 1920; Section 52(2) of that Statute enacted that the profits to which the tax was applicable were the profits of a British company carrying on any trade or business; and, by Section 53(2) profits should be the profits and gains of a trade would be determined for the purposes of Schedule D of the Income Tax Acts, provided that profits should include, in the case of mutual trading concerns, the surplus arising from transactions with members. The decision in Cornish's case that a mutual insurance company carried on business is conceded in the present reference, but the opinions expressed in the Court of Appeal and in the House of Lords in that case, regarding Lord Watson's observation in Styles' case with respect to a mutual assurance company, explain the length to which that noble Lord's observations should be considered as extending.

It was argued by Dr. Gupta that decisions of the English Courts upon the English Income Tax Acts are not usually of assistance to construe the Indian Act. In this connection the observations by the Board in *Raja Bahadur Kamakshya Narain of Ramgarh v. Commissioner of Income-tax, Bihar and Orissa*, are in point. When delivering the judgment of their Lordships of the Judicial Committee, Lord Wright said, at page 188 : "The Indian Income-tax Act, 1922, which was a consolidating Act, is both in its general framework and its particular provisions different from the English Income Tax Acts, so that decisions on the English Acts are, in general, of no assistance in construing the Indian Acts. But in some fundamental concepts reference may be to some extent usefully made to English decisions, in particular as to the meaning of the word income". I venture to include the words "profits" and "gains" as being included in the effect of the above observation.

In the present reference the Fund is a mutual company which, it is admitted, carries on the business of life insurance, the transactions of insurance are effected between the Fund and its members from whom the Fund obtains receipts with respect to those business transactions. The Concise Oxford Dictionary defines income as "periodical receipts from one's business." In the judgment of the Board in *Commissioner of Income-tax v. Shaw Wallace and Company*, it is stated at page 212 that "income, their Lordships think, in the Act (the Indian Income-tax Act, 1922) connotes a periodical monetary return coming in with some sort of regularity, or expected regularity, from definite sources." The annual payments by the members to the Fund are covered by the above observations. Whilst as its Memorandum of Association provides, the income of the Fund shall be applied solely towards the promotion and objects of the company and no portion shall be paid direct to its members, I am unable to see that there cannot be profits upon the transactions between the Fund and its members or that there is no income derived by the Fund from its business. At page 212 in *Shaw Wallace's* case, it was observed that the Act does not define "income" but expands it into "income, profits and gains"; this expansion is a matter of

words and not of substance. The decision in Styles case as explained by the Court of Appeal and in the House of Lords in Cornishs case, was not that there were no profits made by a mutual company out of transactions with its members but that there were no profits assessable to tax. The particular facts in Styles case were that the balance of the receipts from members not required and used for the purpose for which those moneys were subscribed, was returned to the members; but, it is conceded in the present reference, although there is no direct return of the unused part of the members subscriptions, the transactions are mutual dealings and, as such, those receipts, or the surplus from them, are not taxable. Styles case, as explained by Cornishs case, is not an authority that a mutual company does not make profits out of transactions with members, the decision was that profits from those transactions are not assessable to tax by reason that, in effect, they arise out of transactions with itself. In my opinion, since the transactions between the mutual insurance company and its members arise out of the business which it carries on, any surplus therefrom is income or profits and a surplus from members subscriptions is income and profits, but, by reason of the nature of the receipts being mutual dealings, such income and profits are not assessable to income-tax. Since the Fund derives profits from its insurance business which are ascertained by periodical actuarial valuation, it follows that rule 25 applies to the Fund.

Now as to the contention that rule 25 is not the sole method of computation of the income, profits and gains of a life assurance company and that Section 8, 10 and 12 of the Act are not excluded nor abrogated by the rule. This argument appears to suggest that the department can ignore the rule and utilise the above, and other, sections when it suits them or when they wish to do so. By section 3, tax shall be charged in one year in respect of the income, profits and gains of the previous year but the section provides, this is "subject to the provisions of the Act." Sub section (1) of Section 59 empowers the Central Board of revenue to make rules for the purpose of the ascertainment and determination of any class of income; by sub-section (5) the rules made under the section shall have effect as if enacted in the Act; and by sub-section (2) the rules may prescribe the manner in which and the procedure by which the income, profits and gains shall be arrived at in the case of, by clause (ii), insurance companies. The Income-tax Rules, including rule 25 which relates to an Indian life assurance company, and rule 33, which attracts the provisions in rule 25 to a non-resident life assurance company having business in India, were made in pursuance of Section 59; rule 25 is in effect, a provision of the Act and is mandatory in its terms; it provides that the income, profits and gains of Indian life assurance companies, whose profits are ascertained by periodical actuarial valuation, shall be the average annual net profits disclosed by the last preceding actuarial valuation. Since Section 3 is subject to the provisions in the Act, of which rule 25 is one, the provisions, in the rule prevail over those in the section. When a life assurance company ascertains its profits by actuarial valuation, the amount of the average annual net income, profits and gains disclosed by the valuation is the amount for the

purpose of assessment to income-tax, which amount is not obtained by reference to the income, profits and gains of the previous year. Although Section 6 specifies the several heads of income, including interest on Government securities (falling within Section 8), and other sources (falling within Section 12) which are not included in the other heads (covered by Sections 7, 9 and 10) nevertheless the income has not to be assessed separately under the several heads when the total is ascertained by means of rule 25. The ascertainment under the rule of the average annual net profits for the purpose of assessment to income-tax is substituted for the other methods provided by the above sections. In my view assessment cannot be made pursuant to the sections when the rule is applicable.

The next matter for consideration is whether the investments of the Fund and the income derived therefrom form part of its life assurance business. It was argued they do not and that the dividends or interest must be separately assessed under Section 8 and even assuming that the profits from the life assurance business should be computed according to rule 25 nevertheless the dividends and interest do not come within the ambit of the rule as they do not form part, and are not profits of that business.

One of the objects of the Fund, contained in clause 3 (d) of the Memorandum of Association, is to invest the moneys of the company, not immediately required. Insurance business is unlike most other businesses. An insurer receives payments in return for which an obligation arises, dependent upon the nature of the insurance, to pay money upon the happening of the event against which the insurance is effected and which gives rise to payment having to be made. Sudden, unexpected and large claims may be made for which sufficient sources to meet them have to be available, or the premiums in one year may be inadequate to discharge liabilities as and when they crystallize. Investments by an insurance company for those purposes are essential to enable it to carry on its business, to retain the confidence of the public and also its members, particularly in the case of a mutual company, and to be in a position to fulfill its obligations.

Reports of the decisions in the *Liverpool and London and Globe Insurance Company v. Bennett* are found, before Hamilton, J., in [1911] 2 K.B. 577, before the Court of Appeal in [1912] 2 K.B. 41, and in the House of Lords in [1913] A.C. 610. That was a case of an English Fire and Life Assurance Company which carried on a fire insurance business in the United States and in the Dominion of Canada, it made investments (called class A) in those countries for the purpose of complying with their laws; and also other investments (called class B) to comply with the laws of New York and other laws of the Dominion; it also made certain voluntary investments (called class C), not under legal obligation, but for the purpose of deriving income from funds consisting of accumulated profits acquired in past years but not distributed among the shareholders and the investments were made in order to have a fund easily realisable, if required. Generally it had not

been necessary for the company to realise or expend any part of those moneys for the immediate purpose of carrying on its business as insurer. In each of the three Courts it was held that the investments, including class C, were part of the insurance companys business and the interest derived from those investments was part of the profits or gains of the business. Clause 18 of that companys Memorandum of Association corresponded to clause 3 (d) of the Funds Memorandum; it is provided that one of the objects was to invest moneys not immediately wanted. In respect of Clause 18, Cozens Hardy, M.R., observed, at page 54 of the report in the Court of Appeal, that the object (to invest moneys not immediately wanted) was not a distinct one, the business of the company in all its branches was, in truth, one. In the report in the House of Lords, Lord Parker observed, at page 623 that "obviously moneys invested under this clause (clause 18) are not withdrawn from the business of the company but are retained for the purposes of such businesses, though temporarily invested, so as not to be idle". Elsewhere, at page 623, Lord Parker further observed : "The income and dividends of these investments are in fact treated as receipts on account of those businesses and dealt with accordingly, and the capital thereof is and is intended to be at any time available for the purpose of these businesses. The investments, in fact, constitute a reserve fund, and it is, I think, essential in all such business as those carried on by the appellant company that similar reserve funds of this nature should be accumulated". Lord Mersey observed, at page 621 : "It is well known that in the course of carrying on an insurance business large sums of money derived from premiums collected and from other sources accumulated in the hands of the insurers and that one of the most important parts of the profits of the business is derived from the temporary investment of these moneys" and later "It is, according to my view, impossible to say that such investments do not form part of this companys insurance business, or that the returns flowing from them do not form part of its profits.....I make no distinction between the three classes of investments (A, B and C)."

The fund carries on the business of life assurance and I see no reason why the principles, regarding such business, laid down in Bennetts case, are inapplicable because it is a mutual business. From the decision in that case and the observations by the noble Lords, which I have quoted it emerges that the investments of the fund form part of its insurance business. The profits from those investments are part of the business profits and those profits, as well as other profits, are ascertained by an actuarial valuation. This was done at the quinquennial valuation as on 31st December, 1934. Incidentally this is an additional circumstance which fulfills the requirements of rule 25 for its application to the fund. *National Mutual Life Association of Australasia v. Commissioner of Income-tax, Bombay Presidency and Aden* concerned a non-resident mutual life assurance company which effected 98 per cent. of its total business with members. It was accepted before the Board, in that case, as it was accepted in this reference, that the principles in *Styles* case applied; the head office of the company was in Melbourne and it had two branches in India; rule 35 of the Income-tax Rules makes the provisions of rule 25 applicable to a non-

resident life assurance company, in the absence of more reliable data, to ascertain by a periodical actuarial valuation; the Australasia company made a return of its Indian business based on one years account, which the Income-tax Officer did not consider sufficient and he computed the income, profits and gains, under rule 35, upon its last triennial actuarial valuation. Lord Thankerton, in delivering the judgment of the Board, said, at page 112 : "There can be no doubt that the total income, profits and gains of the company would fall to be computed on the basis of their triennial valuation reports which, in their Lordships opinion, is the most reliable method of computation in the case of a life assurance company. It is the method applied under rule 25 in the case of companies incorporated in India"; later in the judgment, the assessment was criticised because, assuming without deciding, that under rule 35 "premium income" should include premiums received from members, it had ignored the principles in Styles case. In my view the Funds investments and the income derived from them are part of their life insurance business.

Now I come to the matters raised by the third question in the reference, namely, whether the Fund can appropriate its income from investments its non-mutual receipts, which is mainly received after deduction of tax at source, in the first instance, against expenditure and to charge any balance against the members subscriptions, its mutual receipts. If this can be done, the whole or the larger part, of the members subscriptions will be retained as surplus and will be free of income-tax. In this connection, the Advocate-General confined "expenditure" to "management expenses." He argued that a debtor can discharge his liabilities out of such part of his income or receipts as he may choose for that purpose, irrespective of its source; the expenditure of the Fund is in respect of its business, which expenditure, he contended, can be met out of whatever source of income the Fund may decide to devote to it. He relied for this proposition upon some English decisions and drew particular attention to some observations by Pollock, M.R., in *Commissioner of Inland Revenue v. Sterling Trust Ltd.* and he also cited two decisions by the House of Lords, *London County Council v. Attorney-General* and *Edinburgh Life Assurance Co., v. Lord Advocate*. I will refer later to those authorities.

Since the profits of the Funds life assurance business are ascertained by means of a periodical actuarial valuation, rule 25 applies; by this means, the income, profits and gains for purposes of assessment in any year are the average annual net profits disclosed by the last preceding valuation, after making any addition, which the rule specifies, and to which reference is not necessary. All assets and liabilities, including management expenses, are taken into account when computing the valuation and before arriving at the estimated surplus for the period covered by the valuation. In those circumstances the question of an allocation of a special fund or of a particular source of income, out of which the management expenses should be paid, or should be deemed to have been paid does not arise. Allocation or appropriation with respect to payment of management expenses could only arise if rule 25 were inapplicable and if the income-tax

assessment of the Funds life assurance business were properly made pursuant to other provisions of the Act.

Although, in the light of the opinion previously expressed, allocation or appropriation has really become academic in this reference, since considerable argument was directed to a debtors right in that respect, I propose to examine the question but this is upon the assumption that rule 25 is in applicable to a mutual life assurance company.

Mutual dealings arise out of a mutual association. To constitute a mutual association a number of persons associate together to subscribe money for a fund for the purpose of it being spent upon a particular object, and the balance, if any, being returned to the subscribers and proportionately distributed amongst them. This balance is that part of the fund which is not absorbed by the particular object of the subscriptions. Those transactions are mutual dealings and the unrequired balance is the surplus. This surplus is not assessable to income-tax since it arises out of mutual dealings. It is immaterial whether the association is corporated or incorporated. The contributors are entitled to participate in the surplus, not necessarily immediately, and for the time being it may be held in suspense and may be invested pending distribution. Since the subscriptions are given and received to constitute a fund for a particular object that fund must be used for that object. If other moneys, instead of the fund, are spent upon that object and the fund is kept intact and not utilised for the purpose for which it is subscribed and obtained, can it be said that the whole fund is the surplus ? Can moneys other than the fund, be used upon the object for which the fund is subscribed so as to create or increase a surplus which would not exist or not be so large. if the fund had been spent upon the object for which it is subscribed ? In my view, not. A surplus from mutual dealings is not the whole of a fund, which is utilised to pay for the object for which the subscriptions to it are made.

In the present reference the members subscribe to the funds of the General Family Pension Fund. These subscriptions are the mutual dealings with and between the association and its members, which are subscribed for the objects of the association, as set out in its Memorandum of Association. One of the objects is to pay the management expenses out of the funds, Therefore, one object of the subscriptions is to pay those expenses and when received they are readily available for that purpose and should be so utilised. If they are not so spent, they are not used for that purpose. Further, the Fund can, under the Memorandum of Association, invest moneys not immediately required. This must mean that they are to remain invested until needed. The capital of the investments cannot be realised to meet liabilities, e.g., management expenses, when other moneys are available, e.g., members subscriptions. Since the subscriptions are, I would say earmarked for those liabilities to the extent which would be covered by them, if the interest from investments is used to pay for the management expenses and the subscriptions are not used, that

is not dealing with the subscriptions in a correct manner. If other moneys are used to pay for the object for which the subscriptions are received, the whole of those subscriptions is not the surplus after utilisation of the fund for its special purpose.

In the London County Council and Edinburgh cases, in the House of Lords, there arose the meaning and effect of an English enactment, Section 24(3) of the Customs and Inland Revenue Act, 1888, which provides that "upon payment of any interest of money or annuities charged with income-tax.....and not payable or not wholly payable out of profits or gains brought into charge to such tax, the person by or through whom such interest or annuities shall be paid shall payment, and shall forthwith render an account to the Commissioners of Inland Revenue of the amount so deducted, or of the amount deducted out of so much of the interest or annuities as is not paid out of profits or gains brought into charge, as the case may be; and such amount shall be a debt from such person to Her Majesty, and recoverable as such accordingly....."

The London County Council raised money upon the security of its consolidated loans fund out of which it paid dividends and interest upon its consolidated stock and loans made to it. The Council received (a) rents and profits of lands, (b) interest or annual payments, both being charged with income-tax before receipts and (c) money raised by rates, not so charged, It paid the dividends and interest upon its loans out of the above three sources of income, and, when doing so, deducted income-tax from the amounts so paid, it retained the income-tax deducted, so far as the dividends and interest were paid out of the rents and profits from land and from interest, upon which income-tax had been charged; but in respect of the payments made out of moneys raised by rates, (which had not been charged with tax), the Council accounted to the Commissioners of Inland Revenue for the amount of income-tax deducted.

The Edinburgh case concerned a life assurance company, the business of which included granting annuities. The companys co-partnership contract provided that every policy or other obligation should contain a clause declaring that its capital stock and funds should be the only fund policy or obligation. The company had a large annual income derived from interest, dividends and rents from which income-tax was deducted source which was sufficient to pay annuities in full, but this income was not formally appropriated in the books nor was any particular fund specially charged with the payment of the annuities. The company also had an income from premiums. When paying the annuities, the company deducted and retained the amount of tax due in respect thereof.

In the above two cases in the House of Lords, payments were made, of interest upon loans by the London County Council and, of annuities by the Edinburgh Insurance Company, out of income from which tax was deducted before it was received by the payers, or debtors. Each debtor had two sources of receipts charged and uncharged, and sought to allocate the payments to charged

receipts and to retain the amount of tax deduction. It was emphasised, by Lord Macnaghten at page 40 and by Lord Davey at page 42 in the London County Council case and by Lord Atkinson at page 158 in the Edinburgh case, that tax is not payable twice on the same income; at pages 42 and 43 in the London County Council case, Lord Davey pointed out that the Crown receiving tax on the whole income in the first instance from the owner had not further claim against the mortgages or annuitant on whose account the owner is deemed to have paid as well as his own and, at page 45, Lord Davey held that the Council was entitled to retain the deductions in respect of income-tax with respect to payments made out of charged income and to account to the Crown only for income-tax on so much of the payments which were made out of uncharged income. The decision in the Edinburgh case was to a like effect. It was in those circumstances, held that the allocations made were correct. In each of those two cases there was no fund out of which payments should have been made and which had not been used for the special purpose nor were payments sought to be deemed to have come from some other fund.

The observations in the Sterling case upon which the Advocate-General relies, were made by Pollock, M.R., at pages 879 and 880 where he said that in general principle a debtor has a right to say how the money which he is paying shall be applied and that the party paying has the right to apply the payments as he thinks fit; and at pages 881 and 882, where a company had two sources of income, charged and uncharged, it is entitled to assume and deem that it has paid according to the most business - like way of appropriating revenue to expenses. That case concerned corporation profits tax imposed by Section 52 of the English Finance Act, 1920; the proviso to sub-section (1)(b) of the section allowed debenture interest to be deducted from the profits of a company before charging to tax. The company had two sources of income, dividends from other companies charged with corporation profits tax before receipt and profits of its business which had not been charged both of which were paid into one common account. The interest on its debentures was paid out of this mixed fund, which payment the company sought to allocate to the uncharged profits and thus reduce the net income chargeable with tax. The management expenses were also paid out of the mixed fund but this expenditure was not sought to be allocated either to one or to the other of the two sources of income. The company was held to be entitled to allocate payment of debenture interest to its uncharged income. In his judgment Atkin, L.J., as he then was, while concurring with the conclusion, said at page 887 that "It is not a question of any right of a person paying the money to pay out of his own funds, and it appears to me that there is nothing in law to prevent a man from paying from any fund,.....that is a lawful fund". But, at page 888, the learned Lord Justice added : "If the question of liability for instance, depended upon whether a man made a payment out of his professional income or out of his invested income I should have said that that was solved by considering the actual fact whether the money did in fact come out of his professional income or.....out of his invested income. If on the other hand, the question was what were the expenses of his profession, then the fact that he

had charged those expenses to invested income or to some other item of income than his professional income would be irrelevant because he could not prevent the fact of it being an expense of his professional income from being determined properly merely by his making a different account in his book." In this case, again, there was not a fund, apart from the mixed fund, out of which the debenture interest should have been paid and there was no attempt to avoid using a fund for its special purpose.

If the General Family Pension Fund allocated the management expenses to interest upon securities instead of to the members subscriptions, they would not be using the subscriptions upon the purpose for which they are received and out of which the expenses should be paid; but they would be utilising another fund for that purpose which, in the circumstances, is not a lawful fund, since the subscriptions should first be used, and it would be dealing with the expenses in a wrong manner and somewhat in the same way as the example of improper allocation given by Atkin, L.J. Further such allocation would not be the most business-like way of appropriating revenue to expenses subject to which, it would seem, the Master of the Rolls recognised a debtors right to allocate.

The last three decisions in England were made with reference to provisions in English Statutes, which do not find a place in the Indian Income-tax Act, permitting deductions in certain instances; in those cases, the taxpayers did not seek to avoid using receipts ear-marked for particular payments, which payments were sought to be allocated to other receipts. I am unable to find that those decisions afford authority for the fund to allocate payment of its management expenses out of its interest income instead of utilising the receipts from members subscriptions for that purpose.

Lastly, although it is the first question referred, there remains whether an Income-tax Officer is bound to continue to assess a taxpayer upon the same principles followed in previous years. The Advocate-General abandoned the contention raised in that question, that an alteration in the method of assessment in subsequent years cannot be made by reason of the principle of *res judicata*. He argued, however, with respect to the second assessment for 1937-38, that since there was one assessment for that year, a second assessment could not be made and the first one discharged, in the absence of any fresh facts. *Sankaralinga Nadar v. commissioner of Income-tax, Madras*, and *commissioners of Inland Revenue v. Sneath* were cited during the argument. This is not raised by the first question and I do not consider the court is required to express an opinion upon it, or in the circumstances, to give an answer to that question.

I would answer the second question in the affirmative and third question in the negative.

The assesseees are entitled to their costs to be taxed.

ORMOND, J. - The questions raised in this case are of importance. It is true that since the assessments now before us the Income-tax Act has been amended by the inclusion of a new schedule governing computation of the income, profits and gains of insurance companies, and that this schedule has been made directly applicable to mutual concerns. Whether or not certain points now raised in this case may possibly arise also directly or indirectly in connection with the application in future cases of the schedule, we are not now adjudicating on the position as it stands today under the schedule but as it stood before the schedule. The nature of the decision to be arrived at in the present case in any event is one that will make a difference to the extent of large sums to the assessee company.

In spite of the directions (at page 1 of the Paper Book) for one reference (meaning presumably the papers for one case relating to one assessment year) to be printed, this has not been done in any clear simple way. The result is that it is not as easy as it should be to trace the details of the various orders made relating to any one of the years of assessment with which the four appeals before us are concerned. The history of the various assessments actually made is found to be this.

As regards the earlier years of assessment between 1928-29 and 1933-34 (inclusive) :- These were originally made on the company not as a life insurance company at all. Then by an order dated 20th July, 1934, the Appellate Assistant Commissioner acting under Section 31(3)(b) set aside those assessments and directed in effect :-

1. That the assessee company should be treated as a life insurance company.
2. And, accordingly, that it should be assessed under rule 25.

Acting on that decision, the Income-tax Officer then made a revised assessment under rule 25. But in doing so he charged the company to tax on an amount of income, profits and gains represented by the figure of the full ascertained surplus (reduced to an average figure) shown I presume by the actuarial valuation for the last periods of years for which such a valuation had been made. The figure for this for which he charged the company to tax was I understand Rs. 4,13,397. Thereafter by a supplementary further order dated 28th August, 1937, the Appellate Assistant Commissioners gave directions for such revised assessment of the Income-tax Officer to be modified. He directed in effect :-

3. That the principle of non-liability to tax of the mutual receipts of a mutual society as laid down in Styles case should be applied to these assessments for the years 1928-29 to 1933-34.
4. That the assessee company should be given the benefit of the principle of favourable appropriation as he deducted it from the Edinburgh case.

These four points, as I have here noted them, will be seen to be the main points on which all the disputes regarding the various assessments have turned.

The Appellate Assistant Commissioner then states his final decision in relation to these assessment years, 1928-29 to 1934-35, in these words (at page 6) :-

"The excess of expenditure over non-mutual receipts for the quadrennium therefore came to Rs. 2,39,498. From these figures it will be seen that the non-mutual income has been completely absorbed by the expenditure, and in these in this circumstances it must be held that the entire surplus of Rs. 4,13,397 arose from mutual sources of receipts and is therefore not taxable."

For the purpose of the application by him of rule 25 the Appellate Assistant Commissioner took into a account a period of 4 years (it does not appear from the materials before us which 4 years) and worked on figures taken from an account which he refers to as "the Life Fund Account."

The course of reasoning involved in this decision, it will be seen, must I think be this : Take the actual expenditure (Rs. 19 lacs odd) : Pay this first out of the non mutual actual receipts (Rs. 16 lacs odd) as far as these will go thus absorbing them entirely; then pay the remaining balance of the total of expenditure (say Rs. 3 lacs approximately) out of the mutual receipts (Rs. 7 lacs odd); you thus arrive at a resultant balance or surplus said to consist of unused portion of the mutual receipts; then, because these mutual receipts are not taxable you conclude that no tax is payable by the company on these assessment years in any respect. (I shall come back to this).

The assessee company was then assessed in accordance with the foregoing decision of the Appellate Assistant Commissioner for the assessment years 1928-29 to 1934-35. It was also assessed on the same lines for the assessment year 1935-36. Its income for each one of these two assessment years was computed as nil. Moreover refunds were directed to be allowed to it on all income-tax already paid by it by deduction at source in respect of interest received on investments.

In pursuance of that decision of the Appellate Assistant Commissioner the assessee company was after that assessed on precisely similar lines and with similar effect in respect of the assessment years 1936-37 and 1937-38. Its income for each of these two years also was again computed as nil. And it was allowed refunds for any income-tax already paid by deduction at source. The amount of refund ordered (as shown by the original assessment order for 1937-38 dated 25th January, 1938, handed up by counsel by consent) was, inclusive of income-tax and surcharge, Rs. 69,777-14-0.

It may be noted in passing that this sum included both income-tax and surcharge deducted at source during the accounting calendar year 1936 (Rs. 62,385-10-0 and Rs. 7,283-7-0 and also a

sum (Rs. 108-13-0 comprising one fifth on income-tax suffered at source on dividends received in the five year period 1930-1934.

When the time came for assessment for the year of assessment 1938-39, however, the Income-tax Officer (as stated in the assessment of the case) (para. 6) made a change in the method of assessment. He proceeded to make the assessment directly under Section 8 and Section 12 of the Act on separate calculations for "interest on securities" (under Section 8) and for income, profits and gains under the head "other sources" under Section 12. The receipts charged by him to tax under Section 12 were in fact for the most part interest on securities also; but such being interest on non Indian securities brought into British India, as were not covered by Section 8. He made no assessment under Section 10 for profits and gains under the head "business" evidently taking the view, since the assessee was a mutual concern, either that it had no business, or that, apart from the receipts already brought to charge under Section 8 and Section 12 it had no further no taxable profits, on the ground that whatever might in a non-mutual company have been classed as profits and gains of its business would be for this mutual concern, on the application of Styles case, mere mutual dealings not liable to tax. (A copy of this assessment as made by the Income-tax Officer on 16th January, 1941, is printed at page 7 of the Paper Book). The figures were taken by him not from any actuarial report but from figures of actual receipts and actual expenditure as shown in the assessee's accounts during the accounting year from 1st January to 31st December, 1937.

At the same time as making the new assessment for the year of assessment 1938-39, the Income-tax Officer also served on the assessee a notice under Section 34 in respect of the year of assessment 1937-38 for the purpose of reporting that assessment. And he made a revised assessment for the year 1937-38 on the same lines as his new assessment for the year 1938-39. The revised assessment for 1937-38 as then made by him is set out at page 9 of the Paper Book. Both these assessments were made on 16th January, 1941 (the date 1943 on page 10 being a misprint).

From these two assessments for 1938-39 and 1937-38 the assessee appealed to the Appellate Assistant Commissioner.

That appeal was disposed of by an order of the Appellate Commissioner on 19th/23rd December, 1941. The effect of his order then made was :-

1. That these two assessments of the Income-tax Officer should be set aside.
2. Revised assessments for each of these two years should be made applying rule 25.
3. But at the same time, as stated in the statement of case, he also directed that "interest on

securities" should be separately assessed under Section 8. Also that income, profits and gains from "other sources" should also be separately assessed under Section 12, bringing in interest on non-Indian investment brought into India which would not be within Section 8, (allowing a deduction against this head for proportionate expenses of management). A copy of his order is printed at page 15 of the Paper Book.

From this order in respect of both the years of assessment (1937-38 and 1938-39) both parties (the assessee and the Income-tax Officer) appealed to the Appellate Tribunal.

These appeals were disposed of by four different orders of the Appellate Tribunal, being orders in R.A.A. Nos. 76 and 77 and orders in R.A.A. Nos. 83 and 84.

In the R.A.A. Nos. 76 and 77 the two appeals by the Income-tax Officer in respect of the assessments for 1937-38 and 1938-39 were allowed and the Appellate Tribunal directed in effect :-

1. That the order by the Appellate Assistant Commissioner for assessment under rule 25 was wrong.
2. Beyond this the Tribunal merely directed that the Income-tax Officer should re-compute the income "in accordance with law." (The orders dated 28th July, 1942, are printed at page 23 of the Paper Book).

Appeal R.A.A. No. 83 related to the objection raised by the appellant assessee in respect of the assessment for 1937-38 in which the assessee (besides other objections as in the assessment 1938-39) took the objection that the Income-tax Officer was not justified in reopening the assessment under Section 34. The Appellate Tribunal held the Income-tax Officer was justified. (Their order dated 28th July, 1942, is printed at page 24 of the Paper Book).

Appeal R.A.A. No. 84 was an appeal by the assessee company in respect of the assessment year 1938-39 against the order mentioned above of the Appellate Assistant Commissioner dated 19th or 23rd December, 1941. Briefly the contentions of the assessee company raised in this appeal were :-

1. That the coupling of the direction of the Appellate Assistant Commissioner to make the assessment in accordance with rule 25 with another direction to make the assessment of interest on investments under Section 8 and of income, profits and gains from other sources under Section 12 was illogical and illegal.
2. That the company mentioned the Appellate Assistant Commissioner was right in directing

assessment under rule 25.

3. That the assessee was entitled to the benefit of favourable appropriation as laid down in the Edinburgh case; that in pursuance of that principle it should be held that the company had met its expenses first from its non-mutual receipts, absorbing all these, so that any surplus of receipts must be derived from mutual dealings; and that the result should be held to be, as contended by the assessee, that there was finally no taxable income for assessment. (The order dated 28th July, 1942, is printed at page 25 of the Paper Book).

It was ordered that the Appellate Assistant Commissioners direction that the assessment should be made under rule 25 was not correct.

To this extent his order was modified. But except in this respect (which was in fact on a point not taken by the assessee, who wished to have the assessment made under rule 25) the directions given by the Appellate Assistant Commissioner were upheld and the appeal of the assessee was dismissed.

The ever-changing seesaw effect of these various decisions in these long drawn-out proceedings is noteworthy. The first assessment for 1938-39 was originally made only on 16th January, 1941. The decision of the Appellate Tribunal was not reached until 28th July, 1942. The matter now comes before us in February, 1946; nearly 7 years after the end of the year of assessment and more than five years after the original assessment for 1938-39 was in fact made.

Though there is an absence of direct language on certain of these points in the order of the Appellate Tribunal the order may, it seems, be taken to mean

1. That the assessee is to be treated as a life insurance company.
2. That rule 25 is not applicable.
3. That the principle of non-liability of mutual receipts on the authority of Styles case is applicable.
4. That the assessment should be made separately of interest on investments under Section 8 and of income, profits and gains from other sources under Section 12.
5. That the principle of favourable appropriation as laid down in the Edinburgh case is not applicable.

Thereafter two applications were made under Section 66(1) of the Act for the statement of a case by the Appellate Tribunal to this High Court against the decisions of the Tribunal in R.A.A. No.

83 and No. 84 : (see pages 30 and 32 of the Paper Book).

As a result of those applications the Appellate Tribunal on 15th August, 1943, stated a case (page 1 of the Paper Book) in which the following three questions of law were referred by it for the opinion of this High Court.

1. Whether the decisions of the Assistant Commissioner of Income-tax, Calcutta, for the years 1928-29 to 1935-36 are binding upon the Income-tax Officer upon the principles of res judicata or otherwise.
2. Whether the income, profits and gains of the General Family Pension Fund for the year ending 31st December, 1936, should be assessed under rule 25 of the Indian Income-tax Rules in the form then in force.
3. If the answer to (2) is in the affirmative, whether in applying the said rule 25, from the surplus so ascertained the Fund is at liberty to appropriate its non-mutual receipts, that is income from its investments, in the first instance, against its expenditure and to charge any balance of expenditure against its mutual receipts, that is income from members subscriptions, thus leaving a final balance of mutual receipts which are non taxable under the authority of Styles case.

I would first make certain general observations concerning rule 25 :-

For an insurance business the actual receipts and actual expenditure in any given year of account give little real indication of the financial state progress of the business or whether it is heading in the long run towards a profit or a loss. When it is considered that an assured may pay a single lump sum entitling him to receive an annuity payment every year for the rest of his life, it is no proper indication of the solvency or profit of the business to point in one given year to the single large receipt for premium counterbalanced during that accounting year by no outgoing payment at all (which will have to be paid if at all many years later), or to point in another given year to the single small payment for an annuity for that year counterbalanced during that accounting year by no incoming receipt at all (since the premium will have been received many years before). So with all other dealings in connection with life insurance other than actual annuities.

Such reasons, no doubt, prompted the observations of the Board by Lord Thankerton in *National Mutual Life Association of Australasia Ltd. v. Commissioner of Income-tax, Bombay*, when he said (in considering rule 35 in respect of Indian branches of non-resident insurance companies) :-

"There can be no doubt that the total income, profits or gains of the company would fall to be computed on the basis of their triennial valuation reports, which in their Lordships opinion, is the most reliable method of computation in the case of a life insurance company. It is the method

applied under rule 25 in the case of companies incorporated in India."

In order to ascertain their progressive financial position it is the common practice of insurance companies to have actuarial valuation reports made on the business of the company at regular periods, commonly at intervals of five years, four years or three years. It is on these reports also that the scale of their charges for premiums for particular classes of business and the amount of bonus decided to be paid out is worked out and reviewed. The assessee company followed this practice, the actuarial valuation reports in its case being for quinquennial periods. During the year of assessment 1938-39 the last existing actuarial valuation report was that which had been made for the five years ending on 31st December, 1934.

An assessment for 1938-39 under rule 25 thus, though it is a computation of the income, profits and gains of the assessee company for that year for assessment purposes of income-tax, is nevertheless based on figure derived from the actuarial report over the five years 1929-34; from which is in fact calculated, by taking one fifth of a total figure, a figure representing an annual average figure.

One feature of rule 25 is that it contemplates a computation of a radically different nature and founded on a radically different basis to that normally adopted for computation of income under Section 8 or Section 10 or Section 12.

Computation of income whether of interest on investments under Section 8 or of profits and gains of a business under Section 10 or of income, profits and gains from other sources under Section 12 is in every case based on actual receipts or on a surplus of actual receipts over actual expenditure during a particular year of account. This is not so for the computation made under rule 25. Here the computation is based on a comparison between the latest actuarial valuation report and last made previous actuarial valuation report of five years before.

For the purposes of the actuarial valuation report the prospective liabilities and prospective assets of the company are taken at a valuation on a capitalised or discounted basis to represent their valuation at the date of the report, after allowing for the prospects of the length of life of the assured on actuarial life tables. Assuming the company is in a solvent state, a surplus will be shown of the valuation of assets on that date over the valuation of liabilities. A difference can then be struck between the figure for surplus on the current actuarial valuation report and the figure for surplus on the last preceding actuarial valuation report made five years before. Such difference is (subject to minor adjustments) taken for the purposes of income-tax as the total income, profits and gains of the company over the five year period covered by the current actuarial valuation report. And one fifth of this is then taken as the average annual income, profits and gains for that period.

While one particular actuarial valuation report may show as a "surplus", a figure representing difference as on that date between the valuation of potential assets over the valuation of potential liabilities, this is not any measure of income of the assessee for purposes of tax. It is the excess of this surplus shown in the current actuarial valuation report over the surplus shown in the last made previous actuarial valuation report, which has to be taken as the income for the five years covered by the current report for the purposes of income-tax. This is referred to in the observations of Lord Thankerton in the case of National Mutual Life Association of Australasia Ltd. v. Income-tax Commissioner, Bombay, when he remarked :-

"A single valuation report as at the end of the year of account of would obviously not have been sufficient for the ascertainment of profits; it would be necessary to have a valuation as at the terminus a quo..."

It will be seen that the difference (in an upward direction) between the two different figures for surplus at the beginning and at the end of the five year period may depend on elements wholly independent of actual receipts. As an illustration : supposing there are on the books of the company 20 persons of varying ages between the 45 and 55, who, having paid up in full all premiums on their policies, are entitled to receive from the company payments of annuities of varying sums for the rest of their lives, a certain figure is taken as the valuation of the liability of the company on their policies. When the actuarial valuation report for 1929 is made, a figure is taken into account on the debit side representing a single capitalised or discounted liability as at a valuation at the date of that report of all future annual prospective liabilities relative to those assured persons over the period (on life tables) of their expected lives; which may be for varying periods in some cases up to as much as another 20 years or more. This figure is an element (on the debit side) in the calculations of the surplus of assets over liabilities on the date of the actuarial valuation report of 1929, Then suppose all those 20 persons die prematurely in 1930. When it comes to make the actuarial valuation report of 1934 the debit figure for liability of the company in respect of the policies of those 20 persons (now deceased) will have vanished to zero. The difference in the surplus of 1934 from the surplus of 1929 will have been increased (among other elements) by the elimination of that debit figure. By that amount (irrespective of other elements) the profits of the insurance company (if a non-mutual company) will have been increased by the difference between that debit figure as it stood in 1929 and as it now stands at zero, in 1934. Yet there will have been no actual receipts during the 5 year period covered by the report which can be said to be responsible for this profit.

In the actuarial valuation report in addition to taking account of the valuation of prospective assets and liabilities arising from premiums expected to be received and payments expected to be made on policies, account is also taken on the valuation of the assets of the company arising

from its investments as the position is assessed on the date of the report. In addition to receipts or prospective receipts for interest, capital appreciation or depreciation may thus come to be reflected in the report, such as would not be included in an assessment of interest on investments if made under Section 8. If it is correct to hold, as I do hereafter, that for an insurance company such as the assessee company it is an integral part of its business to manage its investments such a result of inclusion as "profits," for the purpose of taxation, of surplus derived from an appreciation in capital value of investments, may very possibly, as it seems to me, come to be held to be not incorrect or anomalous. Should it be found necessary to exclude this element from the final notional figure on which tax to be charged, no doubt the final figure could be adjusted. I am not here concerned with that aspect of the matter. I only refer to this as showing another feature of difference between a computation under rule 25 and a computation under Section 8 (with Section 10 or 12).

It is clear therefore that the computation of income, profits and gains under rule 25 is of a nature very different to the ordinary computation for purposes of Section 8 or Section 10 or Section 12 based on actual receipts and actual expenditure in a particular year. It was having regard to such considerations as these, that for convenience in the course of the hearing we referred to the figure representing the difference between the two surpluses as a "notional figure" representing income. When one-fifth of that figure representing notional income for 5 years is taken, this also is a "notional" figure for one years income, profits and gains. It is this notional figure under rule 25 on which tax is then to be charged. It is convenient to refer to it as a "notional" figure for purposes of distinction from figures relating to actual receipts or actual expenditure.

Another feature of rule 25 is that it contemplates an accounting period radically different from that normal under Section 8, 10 or 12. For assessment under Section 8, 10 or 12 the year of account is taken as the year previous to the year of assessment as is the effect of the following provision of Section 3 :-

"tax.....shall be charged for that year (i.e., year of assessment) ....in respect of all income, profits and gains of the previous year..."

By Section 13 it is also provided that "income, profits and gains shall be computed for the purposes of Section 10, 11 and 12 in accordance with the method of accounting regularly employed by the assessee."

The assessee company kept its accounts by calendar years. So, for the year of assessment 1st April, 1937, to 31st March, 1938, if assessed under Section 8 the income computed would be actual receipts of interest actually received during the accounting year between 1st January and 31st December, 1936. But for application of rule 25, the position would be different. In 1937 the

last quinquennial actuarial valuation report to have been made would be the one of the five years ending on 31st December, 1934. So the computation under rule 25 of income, profits and gains would be based on a difference in the surplus (of potential assets over potential liabilities) at 31st December, 1934, from the surplus at 31st December, 1929; for which the company's actual transactions over these 5 years and of nothing later than 31st December, 1934, would form the basis of calculation. It is clear that none of the actual receipts actually received and none of the actual expenditure actually spent during the accounting year 1st January 1935, to 31st December, 1936, could find any place or reflection in the actuarial report for the quinquennium ending 31st December 1934. Moreover for assessments made under rule 25 the same national figure for average annual income, profits and gains would be worked on for a consecutive period of five assessment years until the next actuarial valuation report came out. Since it is only five earlier accounting years (e.g., 1929-1934 for an actuarial valuation report of 31st December, 1934, for the assessment year 1937-38) which can be reflected in the actuarial valuation report, it comes to this; for any computation made under rule 25 an average of a notional figure based on five earlier accounting years is taken as the basis of assessment instead of an actual figure for one year based on a single accounting year immediately preceding the year of assessment.

In view of what has been said it naturally follows, I think, that a computation under rule 25 is not compatible with and cannot be combined with any computation under Section 8 or 10 or 12. This also I think follows from the language of the rule itself. Its wording is :-

"...the income, profits and gains of the Life Assurance Business shall be the average annual net profits disclosed by the last preceding valuation..."

Now the "profits and gains" of the "business" are what are normally, apart from the rule, assessed under Section 10; the "income, profits and gains" from "other sources" are what are normally assessed under Section 12, and the "interest on securities" is what is normally assessed under Section 8. Since interest on securities is certainly "income", all the three classes of receipts referred to in Section 8, 10 and 12 come within the all embracing expression "income, profits and gains" of rule 25. The only question is whether by describing these in rule 25 as "of the Life Assurance Business" it is intended therefore to exclude interest on securities or income, profits and gains from other sources. In the view I take, as later explained, that the management of its investments is, in the case of a life insurance company, an integral part of the business, it follows, I think, that in a case where rule 25 is applied, the computation of income from interest on securities is intended to be included in the computation made under rule 25 and based on the actuarial valuation report; and that no separate assessment under Section 8 of interest on securities is contemplated. Interest on investments on non Indian companies (such as sterling companies) brought into India which, apart from the rule, might be assessed under Section 12 are

also similarly intended, I think, when a computation is to be made under the rule to be brought in to the same calculation based on the actuarial valuation report as being "income, profits and gains" of the company's "business."

I need here consider whether there might be any receipt other than interest on investment which as outside the business might be open to separate assessment under Section 12. There are no such other receipts concerned so far as I am aware in the present case. Apart from considerations arising on the wording of the rule, it would, I think, also be highly impracticable in any practical working of the rule when rule 25 is applied, and a computation is made under it based on actuarial valuation report, to make any separate assessment under Section 12 in respect of interest on investments. As already observed the investments are taken into account for the valuation in the actuarial valuation report. Not only would there be the ordinary intricacies of calculation in arriving at a figure for their exclusion from the difference in the two surpluses taken at the two dates at five years intervals, but there would be the added difficulty that, while investments and interest therefrom as reviewed over a specific 5 years say between 1929 and 1934, would be being taken into account for the actuarial valuation report, investments (probably different) and interest therefrom during a different period (a later accounting year, say of 1936) would be being taken into account for any assessment under Section 12.

It is clear therefore that the basis of computation for rule 25 is radically different from that under Section 8 or Section 10 or Section 12; that the relative accounting period for an assessment made under rule 25 is radically different from the accounting period for Section 8, 10 or 12; also in my view that it is not contemplated under the Act that there should be any separate assessment of interest on securities under Section 8 conjointly with an assessment of income, profits and gains of the insurance business under rule 25. In my view either rule 25 applies to this case; in that event the assessment is to be made under rule 25 without reference to Section 8, 10 or 12; or it does not; in that event the assessment is to be made under the appropriate provisions of Section 8 and/or 10 and/or 12 without reference to rule 25.

With these general remarks which will I believe enable me to shorten what I have to say later, I will now pass to consider the next point, whether rule 25 is applicable in the case of this mutual insurance company or not.

The main arguments advanced by Dr. Gupta on behalf of the Commissioner of Income-tax as objections to the applicability of rule 25 to this case, if I may summarise them, were in effect : (i) That the assessee company not being a life insurance company for the purpose of the Life Assurance Companies Act of 1912, by reason of its having been expressly exempted from the provisions of that Act by Government Notification, it was not a life insurance company under the contemplation of rule 25; (ii) That the assessee company had no business; since what would have

been insurance business in the case of a non-mutual company was in the present case of a mutual concern mere mutual dealings. Having no business, it accordingly had no profits. Alternatively even it be correct to say that the assessee company carried on insurance business, yet it was precluded by its own article and memorandum of association from making any income, profits or gains from its business. In respect of its mutual receipts, by the rule in Styles case being a mutual concern it could not have profits. And in respect of its interest on investments these were not included in the term "business" mentioned in rule 25; since the management of its investments did not form an integral part of the company's "business". In any event, having no profits, the assessee company was therefore outside the rule. (iii) That, conceding, as he did, that the principle of Styles case was applicable in India, any application of rule 25 did not make sense; and the rule became impossible to do practical application and could not be worked out.

Regarding the first of these objections : In my view rule 25 is not restricted to insurance companies governed by the Act of 1912 for reasons already stated by learned brother. Had this been intended it would have been easy to say so. In my view the rule applies to all insurance companies. The assessee company carries on in my view insurance business and it is company incorporated under the Indian Companies Act, therefore it is an insurance company within the meaning of rule 25.

I pass now to the second of these objections.

Regarding the question whether the assessee company being a mutual concern carries on business, that there had at one time been some degree of controversy on this point is seen from the change of view expressed by Brett, L.J., in his own two judgments; first in inclination of the view in *Smith v. Anderson* and later in *In re Padstow Total Loss and Collision Assurance Association*. Any such controversy has however been set at rest. For authority that is now well settled that a mutual insurance company in respect of its mutual dealings does carry on business, it is enough for me to refer only to the decision in the House of Lords in *Commissioners of Inland Revenue v. Cornish Mutual Assurance Co., Ltd.* Indeed it was in the course of the hearing conceded by Dr. Gupta that the assessee company did carry on business.

Regarding the question whether the assessee company makes profits within the meaning of rule 25, if I may deal with this under the heads of the following 4 different points, the position becomes as I see it clear.

Firstly, it appears to me a correct contention speaking for myself that the profits (or the income, profits and gains) referred to rule in 25 mean taxable profits.

Section 3 makes income-tax chargeable under the Act in respect of all income, profits and gains.

Section 4 provides that save as hereinafter provided the Act shall apply to all income, profits and gains as described or comprised in Section 6 (derived etc. in British India). Section 6 relates to the various heads of income, profits and gains which are chargeable to tax. It follows directly from Section 3 as well as on the general tenor of Section 4 and 6 and of the Act as a whole, in my view that with the exception of cases concerning particular express exemptions the word "profits" and the word "income" when read in the Act must be taken to mean taxable profits and taxable income.

Therefore I do not feel it open to me to say that the word "profits" in rule 25 can be taken in the first instance, when testing whether the rule is applicable or not, to mean profits not liable to tax.

For this reason I do not feel, when applying the rule to a mutual company, to ascertain its income, profits and gains, that you would be justified in making a computation in which you took account of all matters (including in this case mutual dealings) which you would take into account if the company were a non-mutual company. In my view the computation to be made under the rule can only mean a computation of the Income, profits and gains liable to tax. I agree with Dr. Guptas argument therefore this far that the rule then will be a applicable to a company which has or may have profits in this sense of "profits chargeable to income-tax."

Secondly, on the authority of Styles case which, it was conceded by counsel on both sides, is applicable in India, any surplus resulting from mutual dealings in the insurance business of a mutual concern such as the assessee company does not constitute a profit chargeable to income-tax.

Thirdly, it may now be taken, I think, as settled, in view of the decision in the case of Liverpool and London and Globe Insurance Company v. Bennett [1913] A.C. 610 (in the House of Lords) (reported also in [1911] 2 K.B. 577, and [1912] 2 K.B. 41, as to the hearing in the Court of first instance and on appeal) that the managements of its investments is an integral part of the business of an insurance company. If this is so in the case of an ordinary non-mutual insurance company, it must, it seems to me, be equally so in the case of a mutual concern such as the assessee company in the present case.

Fourthly, in the present case it is not suggested that the interest on investments is not income or profits which are liable to tax. This interest is clearly not derived from mutual internal dealings among the members but from dealings with persons outside. The Advocate-General indeed conceded that interest on its investments would be liable to tax. Since the investments are in the case of this insurance company part of its business, it follows that profits from its business do exist.

Since it employs actuarial reports, and is an insurance company, and has business, of which there are or may be profits, in my view rule 25 directly applies in terms on its clear wording.

Since it applies, the computation for assessment should be made under rule 25 and not under Section 8 or Section 12 or Section 10. I may here, mention that Dr. Gupta also contended, even if rule 25 was held at all to be applicable to the assessee company, then :

1. That rule 25 does not provide the only method of computation of the income, profits and gains of the companies with which it deals. That Section 8, 10 and 12 of the Act are neither abrogated nor excluded by rule 25. Therefore assessment separately under these sections is open to the Income-tax authorities as an alternative method of rule 25. And :

2. That application of rule 25 (if at all applicable) was limited to the life assurance business; that this did not include interest on investments; and that assessments for this should be made separately (independently of the assessment if any of the assurance business under rule 25) under Section 8 and Section 12.

The effect if these contentions were accepted would be to justify in their entirety the assessments made by the Appellate Tribunal. For, since the insurance business was mutual, there would be nothing to assess; and if the interest on investments were assessed under Section 8 and 12, there would be no room for any available deductions beyond those allowed by the Income-tax Officer in those assessments as made by him.

In view of what I have already said earlier in this judgment, it is unnecessary for me not to say more as to these contentions concerning an alternative or partial application of rule 25. Holding as I do that for this insurance company the management of its investments is an integral part of its business, and in view of the obligatory wording of rule 25 (by use of the word "shall") and holding as I do that rule 25 is applicable to this case, there is no room in my opinion for any assessment under Section 8 or Section 12 in this case.

The position then is, since the management of its investments forms an integral part of its business, this assessee company has a combined business which includes its mutual insurance business and the management of its investments. On this position rule 25 has to be applied in a manner to achieve computation of profits from that side of the combined business which deals with and produces the profits from investments; but not from that side of the combined business which is concerned with the mutual dealings in insurance.

The real difficulty to my mind arises as to the method of application of rule 25. This is the substance of the third of the objections as I have stated them above. By what method of calculation are the profits and gains of the business to be arrived at so as to exclude from the

computation any receipts which in the case of a non mutual insurance company would be profits but in the case of this mutual concern are not profits and so as to find the taxable profits for the purposes of assessment under rule 25; that is to say "the average annual net profits from the actuarial valuation" and as "disclosed by the last preceding valuation". I agree with Dr. Gupta that the matter presents practical difficulties.

By the question of law referred to this Court we are not asked however to express any opinion as to how this calculation is to be made in detail. Nor are we asked how rule 25 is to be applied in general, but whether it is to be applied. We are however asked one particular question in connection with the method of application of rule 25; that is in effect in question 3, if the rule is to be applied, whether, as contended for by it, the assessee company is entitled to invoke and take advantage of the principle laid down in the Edinburgh case to which, for brevity, I shall refer as the principle of "favourable attribution".

In support of the principle of favourable attribution the learned Advocate-General relied principally on four reported cases, being London County Council v. Attorney-General; Edinburgh Life Assurance Company v. Lord Advocate; Sterling Trust Ltd. v. Commissioners of Inland Revenue and Fentons trustee v. Inland Revenue Commissioners. The general principle for which those cases were cited as authority was, as compactly stated in the judgment of Pollock, M.R., in the Sterling Trust case, as follows :-

".....that where you are considering the business of a company which has two sources of income, the one subjected to tax and the other not, you are entitled to assume and deem that it has paid the money that it ought to pay according to the most business-like way of appropriating the revenue to the expenses; further, that even though that has not been done in fact by any separate allocation of the money, as was done here (that is, in the Sterling Trust case) in the later years by putting it at a special bank, still you are entitled to treat the money as having been paid out of the fund which is most favourable to the company, which is, in this case, the tax-payer."

The same principle was in the Sterling Trust case held to be equally applicable whether the assessee was seeking to show "as the most favourable method of payment for himself" payment out of the taxed income or payment out of the untaxed income. In the Edinburgh case and other cases the assessee was contending that moneys had been paid out of funds already charged or subject to charge. In the Sterling trust case it was the other way about. That this made no difference is clear from the passage in the judgment in the Sterling Trust case of Atkin, L.J., at page 887 when he said : "So far that seems to me to establish what was undoubtedly in all those cases a material fact, namely, that the annuities or the interest whatever it might be, was paid, and paid out of, in that case, the taxed income; and I think the same principles leads one to the conclusion that in this case where the advantage is the other way to the tax-payer, that the

payment of the debenture interest was paid out of the untaxed income."

In the London Country Council case the point arose in relation to Section 24(3) of the Customs and Inland Revenue Act, 1888, because under that section in paying the dividends on their consolidated stock out of the Consolidated Loans Fund the London County Council were bound to account to the Crown for the income-tax which they deducted from the dividends "so far only as the dividends are not paid out of their income which has already been charged with income-tax." The question was therefore whether the dividends they were paying to their shareholders were being paid out of a fund which had already been charged with income-tax or out of a fund which had not been so charged. In the Edinburgh case the question was again a similar question arising in the same way on Section 24(3) of the Customs and Inland Revenue Act of 1888. There it was again a question whether the interest or annuities being paid by the company "had been paid out of profits or gains brought into charge." In the Sterling Trust case the question arose in relation to Section 52(1)(b) of the Finance act, 1920. The terms of the section are set out at page 871 of the report of that case. Under that section tax was only payable "after deducting from the amount of profits any interest or dividends actually paid out of those profits." Section 53 of the Finance Act, 1920 (see page 876), being the section showing how the profits are to be assessed on which the tax shall fall, contains an express proviso that there should not be included in the profits subject to the tax (i.e., the Corporation Profits Tax) "the interest, dividends or income received directly or indirectly from a company which was liable itself to be assessed to corporation Profits Tax in respect thereof." So the question in the Sterling Trust case also was a question similar to that in the other two cases, that is whether the debenture interest paid to the debenture-holders by the company had been paid out of a fund consisting of dividends received from companies already charged (or liable to be charged) to Corporation Profits tax or out of some other fund which in the hands of the company would be admittedly liable to Corporation Profits Tax.

The question then is : is that principle of favourable attribution as laid down in the Edinburgh case and those other cases to which I have referred, to be applied in the present case ? In my view it should not for the following two reasons; firstly, because the main problem here is quite different; secondly, even if the main problem were the same, because the necessity for the assessment in the present case being made under rule 25 entails an assessment on a basis of valuation, which is not dependent on or directly concerned with actual payment, and therefore no question of attribution of payments arises at all. It stands to reason that any principle of attribution entails a notion of attribution of some payment to any particular fund, as having been made from, or as having been deemed to have been made from, that particular fund. And if there are no actual payments to be considered, there can be no process of attribution. I should, to explain myself better, enlarge slightly on these two reasons.

In the first place the question arising in the present case is entirely different to my mind from that which arose in those cases to which the principle of favourable attribution was held to be applicable. There the question was whether or not moneys were being paid by the company to persons entitled to receive payment from the company from a fund of a particular class or from a fund of another class; the question was whether the moneys had in fact been so paid, or whether they should have been deemed to have been so paid. There was no question arising about calculating an amount of profits. Here the question is, what is the amount of the profit made by the assessee ? This entails the question what is the amount of expenses that have been incurred in order to make that profit ?

In this particular case it is true a particular difficulty arises since the total surplus of receipts over expenditure of the assessee is earned from a combined business, part of the operations of which are not liable to income-tax and part of the operations of which are liable to income-tax. Were it not for the complication arising from the combined source of earnings the question would be a simple one; what are the total receipts and what are over expenses ? Nevertheless, the question remains no more than this; what is the amount of the profit made ? for this computation required to be made under rule 25 the assets and liabilities have to be balanced up before any figure for taxable profit is arrived at. There is no taxable profit in existence until the balancing process has been completed. In putting the debits against the credits in order to ascertain the profit, and before its ascertainment, there is no question of making a deduction from a profit that has been ascertained or making a payment out of it in the course of its disposal. The assessee cannot therefore here say : "I am making a payment (of management expenses or of payments on policies) out of my taxable profits : or out of a particular fund rather than out of my mutually owned monies received."

Suppose a company had two branches in two different cities under two different persons as managers yet there were dealings common to both branches, and each manager was entitled to commission on the profits of his branch : it surely would not meet the cases if the head office told one manger : "the profits of your branch are nil this year because all the expenses both of your branch and of the other branch have in fact been paid out of the receipts of your branch." This simple illustration, though not exactly on all fours with the present case, illustrates what I find it otherwise difficult to put sufficiently forcibly into simple clear words : that (as I see it), attribution of payment has in truth nothing to do with any process for the ascertainment of profit, which must be worked out, and the working out of which must be finished, before the profit has been ascertained. This, it seems to me, was what Lord Atkin was referring to when he said (in the *Sterling Trust Ltd. v. Commissioner of Inland Revenue*) when giving an illustration :-

"If, on the other hand, the question was what were the expenses of his profession, then the fact

that he had charged those expenses to invested income or to some other item if income than his professional income would be irrelevant because he could not prevent the fact of it being an expense of his professional income from being determined properly merely by his making a different account in his book, and I do not think the cases go to any different decision than that."

What is I think a related aspect of the matter was also referred to by Lord Halsbury in the *Gresham Life Assurance Society v. Styles*, when he observed :-

"When once in individual or a company has in that proper sense ascertained what are the profits of his business or his trade, the destination of those profits..... is perfectly immaterial."

The present computation to arrive at a figure for profits (though working here under rule 25 on the basis of the actuarial valuation) is similar, I think, to the problem in the illustration taken by Lord Atkin. Inherent in any question "What are the profits ?" is the question put by him "What are the expenses ?" For profits will be calculated by arriving at a balance of receipts over expenses (or in the present case working on the actuarial report a valuation of assets over liabilities). In either case whether in Lord Atkins illustration or the present case it will to my mind matter not to be slightest how or from what fund the expenses may have been met or the liabilities have been or will be met. The only relevant question is what are the expenses (or liabilities when working as here on the actuarial report) proper to be taken into account.

In the *Edinburgh* and similar cases on which the assessee relies it was a question of following monies to see whether they were monies on which tax had already been paid because if so they were exempt from paying tax again. Here there is no question of following monies to identify them.

In the second place, I would again here emphasize, what I already referred to in my introductory remarks concerning rule 25, that in a computation made under rule 25 no question either of actual receipts or of actual expenditure arises. The matter rests on a footing of assets or potential assets and of liabilities or potential liabilities as reduced to a static valuation figure as on the date of the actuarial valuation report. So there is no question either of actual expenses of management or of actual payments on policies being deducted from any figure in order to arrive at the profits under rule 25. The essence of the principles laid down in the *Edinburgh* case is that what is there being considered are actual payments made could be said to be "attributed to" - in the sense of being paid out of - a particular fund consisting of actual receipts. In this computation now to be made under rule 25, no actual expenditure and no actual receipts are contemplated; since the whole matter rests on a surplus of assets over liabilities on mere valuation figure (taking into account prospective future liabilities and future asset) and on a difference between a surplus at the terminus at the end of a five year period from a surplus at the terminus a quo at the beginning

of the five year period. The surplus itself is only a notional figure. Since there is no question of actual expenditure or actual receipts there can be no question of attributing payment in fact to any particular class or receipts or to any particular fund.

The result is, I hold therefore, that the principle of favourable attribution as exemplified in the Edinburgh case for example, is not applicable to the present case.

This brings me back again to the third objection raised by Dr. Gupta concerning the actual application of rule 25 as a practical proposition in the present case. Is there any difficulty making it so impracticable in application as was suggested by Dr. Gupta as to make it proper for us to hold in spite of its terms, that on a general construction of the Act it is impossible for the legislature to have intended that rule 25 should be applied in such a case as the present ?

There is another aspect of this matter in so far as practicability of application is concerned. Some comment was made in argument, and I think justifiably, in regard to certain of the rulings given in this case by one or other of the Income-tax authorities, that whether or not the ruling was legally or theoretically when analysed correct, yet it was expressed in terms which made it very difficult for the Income-tax Officer when doing the practical work of assessment to know how he was to act. In view of the length of time over which the doubts and disputes over these assessments have been running on, it will be of benefit to the parties, I think, if when giving my ruling in this appeal I give as clear an indication as possible of a course which the Income-tax Officer may adopt when he has to deal with the matter.

Having, on what has been said above, reached the conclusion that there is a combined business, part of the undertaking of which earns profits, liable to Income-tax and part not, and that the assessment has to be made under rule 25, the problem is to separate the two parts, or the earnings of the two parts of the combined business.

Two possible approaches might be adopted. Either a figure is taken from the actuarial report (one fifth of the total difference in surpluses over the five years) representing the annual total receipts or (broadly speaking) income of the company, and a proportionate fraction of this is taken as being that portion of it which represents the profits from the taxable side of the business : that is to say the investments. (This would be allowing in effect the benefit or deduction for a proportion of expenses of management against the interest from the investments since the total expenses of management for the whole business would have been allowed for as liabilities in the actuarial valuation). Or individual figures might be taken from the actuarial report, or from the detailed calculation on which it is based, showing separate individual assets derivable from investments only (excluding assets derivable from mutual insurance dealing.) and from these there might be

debited some proportional fraction of the total liability figures representing expenses of management. In either case a system of proportion is involved in the calculation.

This brings me to what I reckon to be the last point for determination in this case. Is the use of any such system of proportion in the present case prohibited or legally unjustified ?

To hold that none of the companys expenses are to be taken into account, in arriving at the figure for taxable profit, would amount, I think, to holding that the interest on investments was not part of the companys business. It would be the similar thing in the result as taxing the company on its interest on its investments under Section 8 and not in relation to its business under Section 10. To hold, on the other hand, that the whole of the expenses of the companys business may be deducted in full against its interest on investment would be tantamount to holding that the company has no expenses in its insurance side of its business. As at present advised, though this is not part of the question directly referred to us, once it is decided that it is correct in the case of this insurance company to treat the carrying on of its insurance business even though this arises solely out of mutual receipts and mutual payments also as part of its business, it must follow, in my view, that the total expenses of its business must be shared between the non-taxable part of its business, (that is, its insurance work) and the taxable part of its business, (that is, the management of its investments).

I have taken careful note of the somewhat caustic comments of Lord Davey in *London County Council v. Attorney-General*, when dealing with the system of apportionate in the class of cases referred to above; where the question was the question of fact whether money had been paid or not out of a particular fund; where he observed : "The contention is that.....only a rateable proportion ought to be deemed to be paid out of their income from rents or from interest receivable by them from their own debtors. The proposition has the merit of novelty. Admittedly there is no authority for it. The attention of your Lordships was not called to any statutory enactment directing any such procedure, or to any principle of law which prescribes it. On the contrary, the general principle of payment in due course of administration is to pay annual charges in the first place out of annual income." Which is the passage also referred to by Pollock, M.R., in the *Sterling Trust* case.

I have given anxious consideration to the question whether those comments are equally applicable to such a case as the present where the question is one of the calculation of the amount of profits and (within that) of the amount of expenses to be taken into account in earning the profits before the figure for profits is arrived at. This Court would of course be bound by those observations for the exclusion of any system of proportional calculation if the two classes of cases were the same. I have already observed that in my view the principle of attribution laid down in the class of case being considered by Lord Davey is not applicable in the present case.

Lord Daveys remarks regarding the system of proportion were made only in connection with a process of attribution which arose in those cases but does not arise in this case. After giving the matter full consideration it seems to me that those comments are not intended to be applied and are not at all applicable to such a case as the present, where the question is not the source from which certain moneys had in fact been paid or to be deemed to have been paid, but a pure question of calculation of the amount of the profits. As at present advised I see no better alternative as a matter of both of logic, arithmetic and justice than that the Income-tax Officer in applying rule 25 should adopt a system of proportion; by taking first one-fifth of the surplus shown (by a comparison of the two actuarial reports) which would give the figure for total annual profit if this company has been a non-mutual insurance company; and then taking some proportionate part of that figure so as to arrive at a proper figure representing that part of such total annual figure as would represent the portion of taxable profit in the case of this mutual insurance company. It will be for the Income-tax Officer to divide the figures of the relation in which the proportion should be calculated. Such an assessment though based on valuations on the actuarial reports would have a similar effect as allotting (if an assessment had been carried out under Section 10) a portion of the total expenses of the carrying on of the whole combined business of the company to the earning of the taxable profit.

There should be no practical difficulty that I can see in this.

In regard, to the manner in which the questions referred to us should be answered, I agree with my learned brother that the answers should be :-

- (1) Does not arise.
- (2) In the affirmative.
- (3) In the negative.

I would like, however, for myself to add these qualifying or explanatory remarks.

Regarding question No. 2 I understand this question to relate to the year of assessment 1937-38. I wish to reiterate that if rule 25 is to be applied, it will in any event not be the income, profits and gains for the accounting year ending 31st December, 1936, which will be being assessed. No receipts or expenditure shown in that accounting year will at all be taken into account. It will be a notional average annual figure for income, profits and gains for the assessment year 1937-38, which is to be arrived at based on the actuarial report covering the five years between 1st January, 1929, and 31st December, 1934; and the material from which such notional average figure will be calculated will be those five accounting years as reflected in the valuation given in the actuarial report of 1934 read in comparison with the actuarial report of 1929.

Reference answered accordingly.

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