CALCUTTA HIGH COURT

Braithwaite & Co. (India) Ltd

Vs

Commissioner of Income-Tax

(S.C Deb, C.J. D K Sen, J.)

18.07.1975

JUDGMENT

D.K. Sen, J.

1. This reference arises out of the assessment of M/s. Braith-waite & Co. (India) Ltd., a public limited company, within the meaning of the Companies Act, 1956, for the assessment year 1965-66. The facts found as appearing from the statement of the case and the annexures thereto are as follows :On the 2nd May, 1964, the Companies (Profits) Surtax Act, 1964, received the assent of the President and came into force while the corresponding earlier Act, namely, the Super Profits Tax Act, 1963, ceased to be in operation. On the 15th May, 1964, the recommendations of the directors for the ensuing annual general meeting of the assessee was finalised. The statement of the chairman of the assessee to the members was recorded as follows:

> "The profit for the year after providing Rs. 14,19,333 for depreciation and transferring Rs. 7,03,186 to development rebate reserve, amounted to Rs. 1,24,47,705 which shows an increase of approximately Rs. 18 lakhs over the previous year. This result is most encouraging but once again very large sums are required for payment of taxes as, in addition to income and super taxes amounting to Rs. 62,20,706, Rs. 17 lakhs has been provided for payment of surtax, making a total of Rs. 79,20,706 or more than 63% of the profit. It is interesting to note that this provision for payment of surtax is very nearly the same as that for super-tax in the previous year but is, of course, calculated on the increased profit referred to above."

2. The 34th annual general meeting of the assessee was held on the 18th June, 1964, and the recommendations of the directors as contained in the above statement of the chairman were accepted. In the balance-sheet for the year ending 31st December, 1963, Rs. 17,00,000 was shown under the head "Reserve and Surplus" as reserve for surtax appropriation during the year.

3. On the 1st August, 1964, the assessee entered into an agreement in writing with the National & Grindlays Bank Ltd., whereunder the assessee obtained a "term loan" of Rs. 50,00,000. The agreement provided for repayment of the said loan in instalments as follows :Rs.

1. On the 31st day of July, 1967 5,00,000

2. On the 31st day of July, 1968 7,00,000

3. On the 31st day of July, 1969 10,00,000

4. On the 31st day of July, 1970 12,00,000

5. On the 31st day of July, 1971 16,00,000

4. The agreement also provided that if any default would be made by the assessee in payment of any instalment as above then in such cases the whole of the amount then due and owing to the bank on account of or in relation to the said term loan would at once become due and payable.

5. At this stage it will be convenient to consider the scheme of the Companies (Profits) Surtax Act, 1964 (hereinafter referred to as the said Act). The said Act imposes a charge or tax on the chargeable profits of companies. Chargeable profits have been defined in Section 2(5) of the said Act as follows :

> " 'Chargeable profits' means the total income of an assessee computed under the Income-tax Act, 1961 (43of 1961), for any previous year or years, as the case may be, and adjusted in accordance with the provisions of the First Schedule."

6. Section 4 of the said Act, the charging section, provides as follows:

"Charge of tax.--Subject to the provisions contained in this Act, there shall be charged on every company for every assessment year commencing on and from the 1st day of April, 1964, a tax (in this Act referred to as the surtax) in respect of so much of its chargeable profits of the previous year or previous years, as the case may be, as exceed the statutory deduction, at the rate or rates specified in the Third Schedule."

7. Therefore, under the said Act, surtax is charged on the portion of the chargeable profits as exceeded the "statutory deduction" at the rate or rates specified.

8. "Statutory deduction" has been defined in Section 2(8) of the said Act as follows :

" 'Statutory deduction' means an amount equal to ten per cent. of the capital of the company as computed in accordance with the provisions of the Second Schedule, or an amount of two

hundred thousand rupees, whichever is greater....."

9. Rule 1, inter alia, in the Second Schedule to the said Act provides for computation of the capital of a company for the purpose of surtax as follows :

"1. Subject to the other provisions contained in this Schedule, the capital of a company shall be the aggregate of the amounts, as on the 1st day of the previous year relevant to the assessment year, of-

(i) its paid up share capital;

(ii) its reserves, if any, created under the proviso (b) to Clause (vib) of Sub-section (2) of Section 10 of the Indian Income-tax Act, 1922 (11 of 1922), or under Sub-section (3) of Section 34 of the Income-tax Act, 1961 (43 of 1961);

(iii) its other reserves as reduced by the amounts credited to such reserves as have been allowed as a deduction in computing the income of the company for the purposes of the Indian Income-tax Act, 1922 (11 of 1922), or the Income-tax Act, 1961 (43 of 1961);

(iv) its debentures, if any; and

(v) any moneys borrowed by it from Government or the Industrial Finance Corporation of India or the Industrial Credit and Investement Corporation of India or any other financial institution which the Central Government may notify in this behalf in the Official Gazette or any banking institution (not being a financial institution notified as aforesaid) or any person in a country outside India :

Provided that such moneys are borrowed for the creation of a capital asset in India and the agreement under which such moneys are borrowed provides for the repayment thereof during a period of not less than seven years.

Explanation.--For the removal of doubts it is hereby declared that any amount standing to the credit of any account in the books of a company as on the 1st day of the previous year relevant to the assessment year which is of the nature of item (5) or item (6) or item (7) under the heading 'Reserves and Surplus' or of any item under the heading 'Current Liabilities and Provisions' in the column relating to 'Liabilities' in the 'Form of Balance-sheet' given in Part I of Schedule VI to the Companies Act, 1956 (1 of 1956), shall not be regarded as a reserve for the purposes of computation of the capital of a company under the provisions of this Schedule."

10. In its return the assessee included the said sum of Rs. 17,00,000 shown as "Reserve for Surtax" in its capital base and also included a proportionate amount of the said term loan of Rs.

50,00,000 claiming statutory percentages of the said amounts as deductions in the calculation of chargeable profits.

11. The Income-tax Officer treated the said sum of Rs. 17,00,000 as a provision for taxation and held that the same was not includible in the capital base. So far as the term loan was concerned, the Income-tax Officer held that the same was clearly repayable between 31st July, 1967, and 31st July, 1971, i.e., a period of less than 7 years and held that, therefore, it did not qualify to be treated as a capital. The Income-tax Officer also considered the object of the said loan and held that on that ground also the loan did not qualify to be included in the computation of chargeable profits.

12. Being aggrieved by the order of the Income-tax Officer, the assessee went up on appeal before the Appellate Assistant Commissioner. It was contended in the appeal that the reserve of Rs. 17,00,000 was credited as on 1st January, 1964, when there was no law imposing any charge of surtax. There being no such liability at the material date, namely, 1st January, 1964, the question of making any provision against any liability did not arise and the amount was a reserve simpliciter.

13. The Appellate Assistant Commissioner held that at the material time the Super Profits Tax Act of 1963 was in force, and that information was available at the material date that the Surtax Bill was intended to repeal and replace the Super Profits Tax Act, 1963. He held that the amount of Rs. 17,00,000 was set apart by the company to meet a known liability either of the super profits tax or the surtax. A mere label of reserve was, according to him, not enough but the real nature and character of the sums set apart had to be looked into. On such reasons, he upheld the order of the Income-tax Officer and held that the amount in question was not a reserve but in reality a provision for tax and though shown in the balance-sheet under the head "Reserves and Surplus.", in the course of the year the amount was converted into a provision for surtax.

14. So far as the term loan was concerned, the Appellate Assistant Commissioner found that the loan was granted by the bank on the 1st August, 1964, and the final instalment was repayable on the 31st July, 1971, completing the seven year period and thus satisfied the provisions of Rule (v) of the Second Schedule to the said Act. The provision for repayment of the entire amount of loan in case of default in payment of any instalment on the due date, according to him, could not be said to have reduced the normal period of the duration of the loan. The Commissioner also did not accept the interpretation of the Income-tax Officer as to the purpose of the loan. He overruled such objections and allowed inclusion of the loan for the purposes of computation of chargeable profits under the said Act.

15. Both the assessee and the revenue preferred further appeals before the Tribunal from the

order of the Appellate Assistant Commissioner. The assessee, in its appeal, reiterated before the Tribunal that since the Act imposing surtax was not in force on the 1st January, 1964, the reserve could not be a provision for the same and relied on the decision of the Supreme Court in the case of Commissioner of Income-tax v. Mysore Electrical Industries Ltd. [1971] 80 ITR 566. The Tribunal accepted the resolution which was passed by the assessee on the 18th June, 1964, which had a retrospective effect. But the Tribunal also noted that, (a) the meeting took place on the 18th June, 1964, when the Act had come into force and the directors of the assessee had known of it, (b) the Super Profits Tax Act, 1963, was in force, in any event, on the 1st January, 1964, and provision would have to be made for the same even if the other Act was not promulgated. The Tribunal held that the provision was for a known liability and not a reserve though shown under the heading "Reserves and Surplus" in the balance-sheet and upheld the orders of the Income-tax Officer and the Appellate Assistant Commissioner.

16. In the appeal preferred by the revenue against the'decision of the Appellate Assistant Commissioner in respect of the said term loan, the Tribunal held that only the last instalment of Rs. 16,00,000 was to he paid during a period of not less than seven years. The Tribunal held that the first four instalments aggregating Rs, 34,00,000 were provided for in the agreement to be repaid during a period of less than seven years and did not satisfy the requirement of Rule l(v) of the Second Schedule. The Tribunal held that only the last instalment satisfied such requirement and could be included for computation of the capital base. The Tribunal also held that the default clause in the agreement did not affect the duration of the loan.

17. From the above order of the Tribunal, the following two questions have been referred to us under Section 256(1) of the Income-tax Act, 1961:

"1. Whether, on the facts and in the circumstances of the case, the Tribunal was right in holding that the sum of Rs. 17,00,000 being the amount shown in the balance-sheet as on December 31, 1963, as reserve for . surtax could not be included in computing the capital base under the provisions of the Second Schedule of the Companies (Profits) Surtax Act, 1964 ?

2. Whether, on the facts and in the circumstances of the case, the Tribunal was right in holding that only Rs. 16,00,000 out of the loan of Rs. 50,00,000 taken from the bank qualified for inclusion in the capital base under Rule l(v) of the Second Schedule of the Companies (Profits) Surtax Act, 1964?"

18. Mr. Kalyan Roy, learned counsel appearing on behalf of the assessee, contended in respect of question No. 1 that the said sum of Rs. 17,00,000 fulfilled all the tests and conditions of a "reserve" in law as well as in fact. In support of his contentions he cited a number of decisions. First he cited the decision of the Supreme Court in the case of Commissioner of Income-tax v.

Century Spinning and Manufacturing Co. Ltd. . The facts in that case were that in the relevant accounting period, after making provisions for depreciation and taxation, a sum of Rs. 5,08,637 was carried forward in the balance-sheet of the assessee-com-pany. The assessee contended that under the Business Profits Tax Act, 1947, the said sum should be treated as a "reserve" and taken into account for computation of abatement of taxable profits under that Act. The Supreme Court explained the concept of a "reserve" as follows (page 503):

"The term 'reserve ' is not defined in the Act and we must resort to the ordinary 'natural meaning as understood in common parlance. The dictionary meaning of the word 'reserve' is :

'1(a) To keep for future use or enjoyment; to store up for some time or occasion ; to refrain from using or enjoying at once.

(b) To keep back or hold over to a later time or place or for further treatment.

6. To set apart for some purpose or with some end in view ; to keep for some use.

11. To retain or preserve for certain purposes (Oxford Dictionary, Vol. VIII, p. 513).

In Webster's New International Dictionary, second edition, page 2118, 'Reserve' is denned as follows :

'1. To keep in store for future or special use ; to keep in reserve ; to retain, to keep, as for oneself.

2. To keep back ; to retain or hold over to a future time or place.

3. To preserve'."

19. The Supreme Court found on the facts of that case that originally the directors of the company earmarked the sum for distribution of dividend and in a subsequent meeting of the company it was not (sic) decided to make it a "reserve". The Supreme Court held that the said sum constituted a mass of undistributed profits and did not constitute a "reserve".

20. This definition as enunciated by the Supreme Court has been subsequently followed and applied in a number of decisions of different High Courts in the background of different statutes. Mr. Roy cited a number of such decisions. In the case of Commissioner of Income-tax v. Vasantha Mills Ltd. [1957] 32 ITR 237 (Mad), this definition was applied to determine a reserve under the Business Profits Tax Act, 1947, In a decision of this court in the case of Indian Steel and Wire Products v. Commissioner of Income-tax [1958] 33 ITR 579 (Cal), in the context of the Business Profits Tax Act, 1947, Chakravartti C.J. referred to the decision of the Supreme Court and observed as follows (page 584);

"In the case of Commissioner of Income-tax v. Century Spinning and Manufacturing Co. Ltd. , the Supreme Court had occasion to point out how and when reserves were created. They observed that someone possessed of the requisite authority must make a declaration or give some indication that the manner of the disposal of or the destination of the amount in question is that it is being carried to reserve. That was looking at the question of the creation of a reserve from the procedural point of view. We are concerned in this case with the nature of a reserve. If I may refer to the definition given in Murray's Oxford Dictionary to which the Supreme Court also referred, but only to give the various meanings of the word 'reserve' as a verb, the meaning as a noun is given as follows:

'Something stored up, kept back, or relied upon, for future use or advantage; a store or stock.' An illustration of such use of the word 'reserve' is drawn from Political Economy by Rogers and the following sentence is quoted :

'It is a maxim in business that a man...should have a hoard or reserve from which he can draw, when the times are untoward.' Apart from the dictionary meaning of the word 'reserve' I think it can hardly be disputed that nothing can be reserved unless it has been reserved or laid by or stored for use or application in a future contingency which is anticipated as certain or likely. In the actual administration of companies also a part of the surplus profits is removed from the immediate business of the company by way of a provision against future contingencies and a reserve is thus created, although after being carried to the reserve, the amount in question may be invested or re-employed in the business, if the articles so permit."

21. Mr. Roy next cited another decision of the Supreme Court in the case of the first National City Bank v. Commissioner of Income-tax . In this case, the assessee, a non-resident bank, incorporated under the laws of the United States of America, followed a system of accounting adopted by the American banks and in conformity with the Treasury Rules of the U.S.A. had set aside and transferred the net profits of each year, after provision for expenses, taxes, dividend and reserves, to an account named "undivided profits". The relevant American statute permitted such allocation to be treated as part of the capital funds of the bank. It was found as a fact that the amount transferred to the "undivided profits" account was available for continuous future use in the business of the bank. The question arose whether this amount could be treated as a reserve for the purposes of calculating abatement under the Business Profits Tax Act.

22. The Supreme Court reiterated the definition of a "reserve" in the Century Spinning's case and further laid down that the true nature and character of a sum designated as a reserve was to be determined with reference to the substance of the matter. The Supreme Court held that under the foreign statute the sum kept under the head "undivided profits" was an integral part of the capital structure and should be treated as part of the capital fund.

23. Mr. Roy further cited the following decisions where the concept of reserve was considered in the context of the Super Profits Tax Act, 1963 :

(a) a decision of the Allahabad High Court, in the case of Commissioner of Income-tax v. Security Printers of India (P.) Ltd. ;

(b) another decision of the Allahabad High Court in the case of Commissioner of Income-tax v. Hind Lamps Ltd. ;

(c) another decision of the Allahabad High Court in the case of Commissioner of Income-tax v. British India Corporation (P.) Ltd. ;

(d) a decision of the High Court of Madras in the case of Commissioner of Income-tax v. Indian Steel Rolling Mills Ltd. ;

(e) another decision of the High Court at Madras in the case of Nagammal Mills Ltd. v. Commissioner of Income-tax [1974] 94 ITR 387;

(f) a decision of the Punjab and Haryana High Court in the case of Commissioner of Income-tax v. Hindustan Milk Food Mfg. Ltd. [1975] 98 ITR 517;

(g) an unreported decision of this court in I.T. Reference No. 262 of 1969, in the case of Braithwaite and Co. (India) Ltd. v. Commissioner of Income-tax (since reported in [1978] 111 ITR 729) the same assessee as in this case. In these cases the High Courts considered the nature of respective allocations made by the companies concerned towards taxation, unclaimed dividend, gratuity, bonus and development reserve and proposed dividend, for the purpose of determining whether the same should be treated as reserves for the purpose of computation of capital under the earlier Super Profits Tax Act, 1963. The decision of the Supreme Court in Century Spinning's case was considered and applied in all these cases. The decision of this court in the case of Indian Steel and Wire Products [1958] 33 ITR 579 (Cal) was also referred to and relied on. These cases do not advance the contentions of the assessee any further. It cannot be said that the provisions of the earlier Act of 1963 are in pari materia with the provisions of the Companies (Profits) Surtax Act, 1964, particularly in view of the Explanation to Rule 1(a) of the Second Schedule to the latter Act which was not there in the earlier Act.

24. The only decision cited which considered the Companies (Profits) Surtax Act, 1964, was in the case of Commissioner of Income-tax v. Peria Karamalai Tea & Produce Co, Ltd, . In this case, an amount standing in the account of the assessee-company to the credit of "retirement gratuity reserve" was claimed to be a reserve for the purpose of calculation of capital under the Act. The Kerala High Court, after reviewing the earlier decisions held, following the decision of

the Supreme Court in Century Spinning's case , that any sum of money kept back for future use for a purpose, general or specific, would be a reserve. A reserve for a specific purpose was as much a reserve as for a general purpose. But it was held that a reservation in regard to payment to be made on account of liabilities which have already arisen could not be properly termed "reserve" in the above sense. In contrast it was observed that a reserve made for a specific purpose, not to meet existing liabilities but as a prudent provision for a future liability, which might arise, would not be a "provision" to meet the liabilities.

25. The Kerala High Court also considered the Explanation under Rule 1 of the Second Schedule to the Companies (Profits) Surtax Act, 1964. In that case, the revenue sought to include an allocation for "retirement gratuity reserve" under items shown under the head "current liabilities and provisions" in the statutory form of the balance-sheet in view of the entry No. 10 therein as provision for contingencies and item 5 of the foot-note under that head which referred to other moneys for which a company is contingently liable.

26. The High Court held that this liability for gratuity was not a current liability as it could not be said to have arisen within the year in question. Item No. 5 of the footnote in the statutory form could not include any liability that has not accrued and was not in existence. The High Court concluded that this amount under the heading "Provisions for gratuity" was in the nature of "other reserve ".

27. To distinguish between the concepts of "provision" and "reserve", further, Mr. Roy referred to the Companies Act, 1956. Regulation 87 in Schedule I of the Companies Act provides as follows :

"(1) The Board may, before recommending any dividend, set aside out of the profits of the company such sums as it thinks proper as a reserve or reserves which shall, at the discretion of the Board, be applicable for any purpose to which the profits of the company may be properly applied, including provision for meeting contingencies or for equalising dividends ; and pending such application, may, at the like discretion, either be employed in the business of the company or be invested in such investments (other than shares of the company) as the Board may, from time to time, think fit.

(2) The Board may also carry forward any profits which it may think prudent not to divide, without setting them aside as a reserve."

28. He submitted that under this regulation, the terms "reserve" and "provision" were inter-changeable. The term "reserve" had a wider connotation and necessarily included all provisions. He further relied on Part III of Schedule VI to the Companies Act, 1956, where Parts I and II of

Schedule VI of the Companies Act (which are relevant in the context of the Companies (Profits) Surtax Act, 1964) had been interpreted. Rule 7, Part III, Schedule VI, provides as follows :

"(1) For the purposes of Parts I and II of this Schedule, unless the context otherwise requires,--

(a) The expression 'provision' shall, subject to Sub-clause (2) of this clause, mean any amount written off or retained by way of providing for depreciation, renewals or diminution in value of assets, or retained by way of providing for any known liability of which the amount cannot be determined with substantial accuracy;

(b) the expression 'reserve' shall not, subject' as aforesaid, include any amount written oft or retained by way of providing for depreciation, renewals or diminution in value of assets or retained by way of providing for any known liability ;

(c) the expression 'capital reserve' shall not include any amount regarded as free for distribution through the profit and loss account; and the expression 'revenue reserve' shall mean any reserve other than a capital reserve ; and in this sub-clause the expression 'liability' shall include all liabilities in respect of expenditure contracted for and all disputed or contingent liabilities. (2) Where-

(a) any amount written off or retained by way of providing for depreciation, renewals or diminution in value of assets, not being an amount written off in relation to fixed assets before the commencement of this Act; or

(b) any amount retained by way of providing for any known liability is in excess of the amount which in the opinion of the directors is reasonably necessary for the purpose, the excess shall be treated for the purposes of this Schedule as a reserve and not as a provision."

29. Mr. Roy submitted that under the Companies Act, it was possible for the directors to allocate the profits available to a company in three different manners. Firstly, the profits could be distributed as dividends. Secondly, such profit could be carried forward without distributing the same by way of dividend and without setting them aside as a reserve. Thirdly, such profits or any portion thereof could be set aside as a reserve.

30. According to him the profits set apart for a reserve must be referable to a particular purpose of the company. If the profit set apart was earmarked for providing for any known liability then such a reserve would be in the nature of a provision but if it was intended to be used for a future purpose not presently ascertained but anticipated in praesenti then it could not be a provision but must be treated as a reserve.

31. In the form of the balance-sheet contained in Part I of the annexure to Schedule VI of the Companies Act there was a specific heading "Reserve and Surplus", the item No. 4 in which was "other reserve, specifying the nature of each reserve and the amount in respect thereof" and items Nos. 5, 6 and 7 were respectively, (a) surplus, i.e., balance in the profit and loss account after providing for proposed allocation, namely, dividend, bonus or reserve, (b) proposed addition to reserve, and (c) sinking fund.

32. Correspondingly, under the head "Current Liabilities and Provision", sub-head "Provision" came, (1) provision for taxation; (2) proposed dividend; (3) for contingencies; (4) provident fund scheme; (5) for insurance and similar several bonus schemes ; (6) other provisions.

33. Mr. Roy contended that for the purposes of Rule 1 of the Second Schedule of the Companies (Profits) Surtax Act, 1964, the taxing officer had to consider whether any amount standing to the credit of any account in the books of a company was in the nature of items No. 5, 6 or 7 in the statutory form of the balance-sheet under the heading "Reserve and Surplus". The taxing officer had also to ascertain whether such a credit could be any item under the sub-head "Provision" in the statutory form referred to above. If such credit was found to be of the nature of the above three items under the head "Reserve and Surplus" or was found to be an item under the head "Current Liabilities and Provisions" only then it should not be treated as a reserve. Otherwise, if the same was not carried forward as undistributed profit it must be treated as a reserve.

34. In construing the Explanation in the said rule in the Second Schedule of the Act, Mr. Roy contended that the words "of the nature" governed only item No. 5, 6 or 7 under the head "Reserve and Surplus" and not the items under the head "Current Liabilities and Provisions". In respect of the latter the allocation in question had to come specifically within such items in order to be excluded from computation of capital. This contention does not appear to be of substance. In the Explanation, the preposition "of" appears before the items under the heading "Reserve and Surplus" as also before the words "any item" under the heading "Current Liabilities and Provisions". It appears, therefore, to us that the taxing officer in applying the Explanation has to consider the nature of the items as appearing under the heading "Reserve" as also of the items under the heading "Provision".

35. Mr. Roy submitted that in the instant case the resolution of the annual general meeting passed on the 18th June, 1964, had a retrospective effect and the allocation must be treated as being effective on the 1st day of the relevant year, i.e., 1st January, 1964, when the Act in question, namely, the Companies (Profits) Surtax Act, 1964, was not in existence.

36. In support of this contention Mr. Roy relied upon the decision of the Supreme Court in the case of Commissioner of Income-tax v. Mysore Electrical Industries Ltd. [1971] 80 ITR 566.

This was also a case involving the present Act, namely, the Companies (Profits) Surtax Act, 1964. The facts of this case were that on the 8th August, 1963, the directors of the asses- see in their report to the shareholders proposed a number of appropriations out of the profits of the year ending on the 31st March, 1963. The appropriations were under the headings "Plant Modernization and Rehabilitation Reserve, Loan Redemption Reserve, Reserve for the Development Rebate, Dividend Reserve and Reserve for Super Profits Tax". The asses-see claimed that all the above appropriations should be computed as reserves for the purpose of calculating the capital base of the company. The Mysore High Court held that from the Explanation to Rule 1 of the Second Schedule to the Act it was clear that the amounts standing to the credit of any account which was in the nature of any item under the head-

ing "Current Liabilities and Provisions" in the column relating to the liabilities in the form of balance-sheet shall not be recorded as a reserve. Applying this test the High Court held that the amounts standing to the credit of "Dividend reserve" and "Reserve for super-tax" were in the nature of items "Provisions for taxation" and "Proposed dividend" and, therefore, could not be regarded as a reserve for the purpose of the computation of capital. The High Court further held that the amounts appropriated for "Plant modernization and rehabilitation reserve", "Loan redemption reserve" and "Development rebate reserve" were accounts in the nature of reserve. The last three items had been disallowed by the taxing officer and the Appellate Assistant Commissioner on the sole ground that the board of directors made the appropriations on the 8th August, 1963, and not on or before the 1st April, 1963. The Mysore High Court held that it was not possible for a company to make any appropriation out of the profits of any year before the close of the year of accounting and though the board of directors in their report to the shareholders made the appropriation after 1st April, 1963, the appropriations were effective from the 1st April, 1963.

37. The sole contention on behalf of the revenue before the Supreme Court in appeal was that such appropriations having been made on the 8th August, 1963, would not be treated as components of capital on the 1st day of the previous year in terms of Rule 1 to the Second Schedule. The Supreme Court in its judgment held as follows--See :

"It is well known that the accounts of the company have to be made up for a year up to a particular day. In this case that day was the 31st March, 1963. If it was reasonably practicable to make up the accounts up to the 31st March, 1963, and present the same to the directors of the respondent on April 1, 1963, they could have made up their minds on that day and declared their intention of appropriating the said and other sums to reserves of different kinds. But the fact that they could not do so for the simple reason that the calculation and collection of figures of all the items of income and expenditure of the company for the year ending March 31, 1963, was bound

to take some time cannot make any difference to the nature or quality of the appropriation of the profits to reserves as determined by the directors after the 1st of April, 1963, Their determination to appropriate the sums mentioned to the three separate classes of reserves on the 8th August, 1963, must be related to the 1st of April, 1963, i.e., the beginning of the accounts for the new year and must be treated as effective from that day."

38. Relying on the above decision of the Supreme Court, Mr. Roy contended that in this case the said amount of Rs. 17,00,000 which was reserved for payment of surtax at the annual general meeting of the asses-see on the 18th June, 1964, must be related back to the balance-sheet of the company as on the 31st December, 1963. Therefore, on the 1st January, 1964, it had to be ascertained what was the nature of this allocation. The resolution of the company became effective on the 1st January, 1964, and on that date this amount of Rs. 17,00,000 stood separated from the profits of the company and, therefore, could not form part of the profits. It also could not be stated to be a provision for taxation, as, on the 1st January, 1964, the Companies (Profits) Surtax Act, 1964, had not come into operation and, therefore, on the 1st January, 1964, it could not be stated that the said amount was in the nature of a provision for any known liability. This allocation, on the other hand, fulfilled all the tests of a reserve in its ordinary meaning. It is nobody's case that this amount was in the nature of items Nos. 5, 6 and 7 under the heading "Reserve and Surplus" in the statutory form of the balance-sheet nor could it be des- cribed as any of the items under the heading "Current Liabilities and Provision" in the said statutory form. It followed that this amount must be treated as a general reserve kept for future use and must be included in computing the chargeable profits of the assessee for the purpose of surtax under the 1964 Act.

39. Mr. Balai Pal, learned counsel appearing on behalf of the revenue, contended on the other hand that this amount of Rs. 17,00,000 was specifically reserved for the purpose of payment of surtax at a time when the present tax, namely, the Companies (Profits) Surtax Act, 1964, came into existence and, therefore, the said allocation was really in the nature of a provision for taxation and directly came under the relevant item under the heading "Current Liabilities and Provision" in the statutory form of a balance-sheet.

40. Mr. Pal contended, in the alternative, that there was no reason why this allocation could not be stated to be an item in the nature of a provision for contingencies in the statutory form under the heading "Current Liabilities and Provisions".

41. On careful consideration of the respective submissions.it appears to us that in view of the law laid down by the Supreme Court in the case of Mysore Electrical Industries Ltd. , the contentions of the assessee cannot be accepted. It cannot be disputed that the accounts of the company may be made up for a year up to a particular date at a later point of time. A company is entitled in law

to finalise later as to what was the position of its accounts as up to a particular earlier date. A company can similarly finalise its appropriations for various purposes including reserves and provisions at a later date with retrospective effect. Such determination to appropriate must be related back to the day up to which the accounts are finalized and such determination including appropriations towards reserve and provision must be treated as being effective from that date.

42. It appears to us that once such determination and appropriation are made the same finally determine the character of the allocation and if it relates back to an earlier point of time then it relates back effectively in all respects and retain its nature and character.

43. A company can take the advantage of retrospective effect of its determination of appropriations but it cannot then contend that by being retrospectively effective the nature of the appropriation will change. If the resolution of the directors to appropriate for surtax in August, 1964, is effective from the 1st January, 1964, then it is effective for all purposes and the nature of the appropriation, i.e., its character as a provision for a known liability cannot undergo a metamorphosis and change into an appropriation of a different character.

44. In this view of the matter, we are of the opinion that the said sum of Rs. 17,00,000 shown in the balance-sheet as on the 31st December, 1963, as a reserve for surtax was in the nature of a provision for taxation within the meaning of the Explanation in Rule 1 to the Second Schedule of the Act and could not be included in computing the capital base of the company for the purpose of determination of chargeable profits.

45. On question No. 2, Mr. Roy contended that the said loan of Rs. 50,00,000 was a single loan. The fact that the said loan would be repaid in a number of instalments would not convert it into a number of separate loans of different amounts. The agreement in respect of the loan specifically provided that repayment would start from the 31st of July, 1967, and end on the 31st July, 1971.

46. Mr. Roy submitted that the period calculated from 1st August, 1964, to 31st July, 1971, was a complete period of 7 years and the agreement specifically provided for the repayment of the loan during this period and as such this loan came within the four corners of the proviso to Sub-rule (v) of Rule 1 in the Second Schedule to the Act. Mr. Roy contended that the Tribunal was not right in holding that only the last instalment of Rs. 16,00,000 payable on the 31st July, 1971, qualified to be included in the capital base of the company. Either the entire loan came within the proviso or it was excluded entirely. A part of the loan could not be held to fall within the scope of the proviso.

47. Mr. Pal, on behalf of the revenue, contended on the other hand that the loan was repayable between 1st August, 1964, and the 31st July, 1971, in five instalments. He submitted that this

period was only five years and, therefore, was excluded from the proviso in Rule 1(v). This contention of Mr. Pal does not appear to be of much substance. The proviso specifically speaks of repayment of a loan duiring a period of not less than seven years. The period of seven years should be calculated from the date of the loan. If the contention of Mr. Pal is correct then any loan which is to be repaid after seven years but at a time and on a particular day will never be included in the proviso. It does not appear to us that such loans were intended to be excluded from the proviso.

48. Mr. Pal next contended that in calculating the period of seven years one day should be excluded and the seven years in the instant case would be completed on the 1st August, 1971, and not on the 31st July, 1971. In support of his contention Mr. Pal relied on a decision of the Supreme Court in the case of S. S. Gadgil v. Lal & Co. . In this case, the Supreme Court was considering Section 34(1) of the Indian Income-tax Act, 1922, which was amended by the Finance Act, 1956, with retrospective effect from 1st April, 1956. By the amendment the original period of limitation was extended from one year to two years from the end of the assessment year concerned. On 12th March, 1957, a notice in respect of assessment year 1954-55 was issued under this Section and a question of limitation arose. The Supreme Court held that the assessment year in question, i.e , 1954-55, ended on 31st March, 1956, under the unamended Act and though the amending Act retrospectively extended the period to two years with effect from 1st April, 1956, the proceedings which were available before the amendment had become barred before that date. This decision does not in our opinion apply in the facts and circumstances of this case.

49. No doubt, under Section 9 of the General Clauses Act, in computing a period of time prescribed by a statute one day has to be excluded, but in the instant case, we are construing the period of repayment provided in an agreement. We cannot import Rules of computation from the General Clauses Act for computing periods as contained in agreements. There are statutes which provide for computation of time in certain agreements. The Transfer of Property Act in Section 110 provides for computation of time limited by a lease. Mr. Pal could not cite any particular statute which could be called in aid for computation of time in the instant case.

50. In the premises, we do not accept the contention of Mr. Pal and we hold that the agreement in specific terms provided for the repayment of the loan during a period of not less than 7 years.

51. Lastly, Mr. Pal contended that the agreement provided for repayment of the entire amount of loan in the case of default in payment of any of the instalments covenanted. He submitted that this default clause in the agreement provided for repayment of the loan within a period of less than seven years. In this connection, Mr. Pal relied on a decision of this court in Jadab Chandra Bakshi v. Bhairab Chandra Chuckerbutty, ILR [1904] 31 Cal 297 as also on an English decision,

Lahshmijit v. Faiz Mohammed Khan Sherani [1974] AC 605 (PC). These decisions are authorities for the proposition that in cases of repayment by instalments where the entire amount became payable in case of a default then the period of limitation for recovery of the entire amount starts to run from the default. These decisions according to us are not of much assistance in the instant case.

52. Here, the default clause comes into operation only in a contingency, i.e., in the case of a default in payment of an instalment. Till that contingency arises the entire amount will not become repayable at once and the default clause would remain in abeyance. The agreement provides that the first instalment is to be paid in 1967. It has not been found that the assessee-company had committed any default and there was no question of any default before 1967.

53. If Mr. Pal is correct in his contentions then it follows that the Tribunal committed an error in even allowing the last instalment of Rs. 16,00,000 payable on the 31st July, 1971, to be included for computation of the capital base of the company. The revenue has not challenged this finding of the Tribunal and has not raised any question against this finding. The dispute before us has been raised by the assessee and is limited to the question whether only the said last instalment should be included under Rule !(v) of the Act or the entire loan should be so included. The question of law which the revenue now seeks to urge has been decided by the Tribunal against the revenue and is now closed. The Supreme Court observed in the case of Commissioner of Income-tax v. Anusuya Devi , that even where a question was before the court, power should not be exercised for re-opening an enquiry on questions of fact or law which is closed by the order of the Tribunal. In the instant case, the revenue has not even sought to refer any question.

54. For reasons discussed above, we cannot accept the contentions of Mr. Pal. This loan must be held to fall within the proviso to Sub-rule (v) to Rule 1 of the Second Schedule to the Act and must be taken into account in order to determine the capital base and/or chargeable profits of the assessee.

55. We answer question No. 1 in the affirmative, in favour of the revenue and question No. 2 in the negative, in favour of the assessee and return our answers accordingly. In view of the divided success, parties will bear their respective costs.

Deb, J.

56. I agree.