

CALCUTTA HIGH COURT

Duncan Brothers and Co Ltd

Vs.

Commissioner of Income Tax

(Dipak Kumar Sen, J.)

24.12.1975

JUDGEMENT

Dipak Kumar Sen, J.

(1.) IN this reference under Section 256(1) of the INcome-tax Act, 1961, at the instance of Messrs. Duncan Brothers and Co. Ltd., the assessee, the effect of a provision made for taxation by a limited company on the computation of its capital for the purpose of the Super Profits Tax Act, 1963, and of the Companies (Profits) Surtax Act, 1964, has to be determined. The relevant assessment years are 1963-64 and 1964-65. The accounting years involved are the years ended 31st December, 1962, and the 31st December, 1963.

(2.) THE facts found and/or admitted in this reference may shortly be stated as follows : For the assessment year 1963-64, the assessee had claimed that in the computation of its capital a provision for taxation Of the amount of Rs. 16,48,888 should be treated either as a part of capital under the head "other reserves" under Rule 1 or as a deduction from cost of investments in terms of Clause (ii) of Rule 1 of the Second Schedule to the Super Profits Tax Act, 1963. This claim was disallowed by the Income-tax Officer. On appeal, the Appellate Assistant Commissioner held that the said provision was only an amount set apart to meet the liability for taxation, considered as accruing on the last date of the accounting year, and could not be treated as a reserve. But the alternative contention that such a provision fell under Clause (ii) of Rule 1 of the Second Schedule to the Super Profits Tax Act, 1963, was accepted and it was held that the said sum of Rs. 16,48,888 on account of this provision for taxation had to be reduced from the cost of investments in computing the capital base. In respect of the assessment year 1964-65 a sum of Rs. 17,52,920 had been laid out by the assessee as a provision for taxation and the assessee claimed that the said amount should either be treated as a reserve or as a deduction in arriving at the net cost of investments under the provisions of the Companies (Profits) Surtax Act, 1964, for the purpose of computation of the assessee's capital. The Income-tax Officer again disallowed the claim of the assessee but on appeal the Appellate Assistant Commissioner upheld such claim on the alternative ground that it was to be deducted from the cost of investments under Rule 2(ii) of

the Second Schedule of the Companies (Profits) Surtax Act, 1964. From the orders of the Appellate Assistant Commissioner in respect of both the assessment years 1963-64 and 1964-65, the revenue went up on further appeal before the Appellate Tribunal. The Tribunal held that the provision for taxation made by the assessee in both the assessment years was neither a "fund" nor a "surplus" and could not be a reserve to form part of the capital. Such a provision being made against a perfected debt did not qualify for any deduction as claimed by the assessee. From the order of the Tribunal the following questions have been referred : For the assessment year 1963-64 : "(1) Whether, on the facts and in the circumstances of the case, the Appellate Tribunal was right in holding that the 'provision for taxation' is not a reserve as to form part of the capital under Rule 1 of the Second Schedule to the Super Profits Tax Act, 1963. (2) If the answer to the above question is in the affirmative, whether, on the facts and in the circumstances of the case, the Appellate Tribunal was right in holding that in the computation of capital the company was not entitled to the benefit of deduction of the amount of 'provision for taxation' from its cost of investments in terms of Clause (ii) of Rule 1 of the Second Schedule to the Super Profits Tax Act, 1963." For the assessment year 1964-65 ; "Whether, on the facts and in the circumstances of the case, the Tribunal was right in holding that in the computation of capital the company was not entitled to the benefit of deduction of 'provision for taxation' from its cost of investments in terms of Clause (ii) of Rule 2 of the Second Schedule of the Companies (Profits) Surtax Act, 1964."

(3.) BOTH super profits tax and companies (profits) surtax are leviable on what is known as "chargeable profits" of a company. This chargeable profit is generally the income of a company as assessed under the Income-tax Act, 1961, subject to certain adjustments and deductions as provided in the said statute. One of the items of adjustment is a deduction of a statutory percentage of the computed capital of the company. The rate of the respective taxes also depend on the excess of the chargeable profits over statutory deductions. The Second Schedule to the Super Profits Tax Act, 1963, contains Rules for computing the capital of a company for the purposes of super profits tax. Rule 1 is as follows : "1. Subject to the other provisions contained in this Schedule, the capital of a company shall be the sum of the amounts, as on the first day of the previous year relevant to the assessment year, of its paid up share capital and of its reserve, 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), and of its other reserves in so far as the amounts credited to such other reserves have not been allowed in computing its profits for the purposes of the Indian Income-tax Act, 1922 (11 of 1922), or the Income-tax Act, 1961 (43 of 1961), diminished by the amount by which the cost to it of the assets the income from which in accordance with Clause (iii) or Clause (vi) or Clause (vii) of Rule 1 of the First Schedule is not includible in its chargeable profits, exceeds the aggregate of--(i) any money borrowed by it which remains outstanding; (ii) the amount of any fund, any surplus and any such reserve as is not to be taken into account in computing the capital under this rule. Explanation 1.--A paid-up share capital or reserve brought into existence by creating or increasing (by revaluation or otherwise) any book asset is not capital for computing the capital of a company for the purposes of this Act. Explanation 2.--Any

premium received in cash by the company on the issue of its shares standing to the credit of the share premium account shall be regarded as forming part of its paid-up share capital. Explanation 3.--Where a company has different previous years in respect of its income, profits and gains, the computation of capital under Rule 1 and Rule 2 of this Schedule shall be made with reference to the previous year which commenced first." ;