

though not to increase it. The document was altered while in the possession of the very person who, as the agent of Anirudhan, brought it to the Bank on both the occasions. Anirudhan must be deemed to have held out Sankaran as his agent for this purpose and this creates an estoppel against Anirudhan, because the Bank believed that Sankaran had the authority. The offer thus remains in its amended form an offer of Anirudhan to the Bank and the Bank by accepting it turned it into a contract of guarantee which was backed by the past consideration on which the offer of Anirudhan was originally based.

In my opinion, the appeal must fail. I would, therefore, dismiss it.

BY COURT: In accordance with the opinion of the majority, the appeal is dismissed. There would be no order as to costs.

Appeal dismissed.

COMMISSIONER OF INCOME-TAX, BOMBAY

v.

JUBILEE MILLS LTD., BOMBAY

(J. L. KAPUR, A. K. SARKAR AND
M. HIDAYATULLAH, JJ.)

Income Tax—Individual members of companies, assessment of—Public substantially interested, meaning of—Group controlling more than 15% voting power—Managing Agents forming such a group—Indian Income-tax Act, 1922(11 of 1922), s. 23A.

Section 23A of the Income-tax Act, 1922, empowered the Income-tax Officer to assess individual members of a company in respect of undistributed assessable income of the company in certain circumstances. The proviso to this section made s. 23A inapplicable to a company in which the public was substantially interested. The explanation to the proviso laid down that a company shall be deemed to be one in which the public was

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substantially interested if the shares of the company carrying not less than 25% of the voting power had been allotted unconditionally to or acquired by the public and were held beneficially by the public. It was found that though the directors of the company's *qua* directors did not hold more than 75% of the shares, the shares held by such directors as were partners in the firm of the Managing Agents of the company together with the shares held by other partners of the Managing Agents and the shares held by the members of the Managing Agency on behalf of minor children exceeded 75% of the voting power.

Held, that the company was not one in which the public was substantially interested and s. 23A was applicable to it. No person could be said to belong to the "public" unless he held the shares unconditionally and beneficially for himself. The words "unconditionally" and "beneficially" indicated that the voting power arising from the holding of those shares should be free and not within the control of some shareholder and the holder should not be a nominee of another. Directors, *qua* directors, were not without the pale of the public as there was nothing that required them to act in unison. What had to be seen was whether there was any individual or a group holding the controlling interest which group acting in concert could direct the affairs of the company at its will. The partners of the Managing Agency constituted a group holding more than 75% of the voting power in the company and they could not be counted as public as they must be taken to act in their own interest in unison".

Commissioner of Income-tax v. H. Bjordal, [1955] 28 I. T. R. 25, referred to.

Shri Changdeo Sugar Mills Ltd. v. Commissioner of Income-tax, Bombay, [1961] 41 I. T. R. 667 and *Raghuvanshi Mills Ltd. v. Commissioner of Income-tax* [1961] 41 I. T. R. 613, relied on.

CIVIL APPELLATE JURISDICTION : Civil Appeal No. 599 of 1961.

Appeal from the judgment and order dated March 13, 1958, of the Bombay High Court in I. T. R. No. 40 of 1957.

R. Ganapathy Iyer and *R. N. Sachthey*, for the appellant.

A. V. Viswanatha Sastri and *I. N. Shroff*, for the respondent.

1962. September 17. The Judgment of the Court was delivered by

HIDAYATULLAH, J.—This is an appeal on a certificate of fitness granted by the High Court of Bombay against the judgment of the High Court dated March 13, 1958, on a reference made by the Income Tax Appellate Tribunal. The Commissioner of Income Tax, Bombay City I, is the appellant and the Jubilee Mills Ltd., Bombay, the respondent. The only question raised in this appeal is the application of s. 23A of the Income-tax Act to the assessee company.

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The assessee company is a limited liability company with a paid-up capital of Rs. 15,25,000/-. Its paid up capital is made up as under :—

1 Lakh Ordinary Shares of Rs. 10 each	Rs. 10,00,000
5,000 Cumulative Preference Shares of Rs. 25 paid-up.	Rs. 1,25,000
4,000 Second Preference Shares of Rs. 100 each fully paid-up.	Rs. 4,00,000

The Second Preference Shares do not entitle the holders to vote. Thus shares of the assessee company carrying votes are 1,05,000. This was the position on June 30, 1947. We are concerned with the assessment year 1948-49 corresponding to the previous year ended on June 30, 1947. In that year, the company was assessed on a total income of Rs. 7,47,639/-. The Income Tax Officer calculated the tax at Rs. 3,27,091, and the balance available for distribution was Rs. 4,20,548. In that year, the company ought, if s. 23A was applicable, to have distributed 60% of the above amount. The company, however, declared dividends which in the aggregate amounted to Rs. 24,750. The Income Tax Officer, with the previous approval of the Inspecting Assistant Commissioner applied the provisions of s. 23 A of the Income Tax Act and held that the company was deemed to have declared dividend of Rs. 3,97,788/-.

The assessee company was being managed by a firm called Mangaldas Mehta & Co. That firm

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consisted of 14 partners of whom seven were the directors of the assessee company. The members of the Managing Agents who were also directors held between them 35,469 ordinary shares and 880 First Preference Shares. The remaining seven members of the Managing Agents, who were not directors of the assessee company, held respectively 41,659 and 370 shares of the two categories. 75 shares were held by Girdhardas & Co. Ltd. to which company admittedly s. 23 A was applicable. Some of the members of the Managing Agency firm held on behalf of their minor children or on behalf of their joint families 9,899 Ordinary Shares and 937 First Preference Shares. The following is a detailed break-up of the share holdings :—

Category 'A'.

Shares held by Directors who are partners in the firm of Managing Agents	Holding of ordinary shares	Share in the partnership of firm of Mg. Agents' firm	Holding of the Ist Preference Shares
1. Shri Homi Mehta	50	8/128	Nil
2. Sheth Mathuradas Mangaldas Parekh	6,466	14/128	273
3. „ Madanmohan Mangaldas	11,052	14/128	273
4. „ Madhusudan Chamanlal Parekh	3,616	7/128	20
5. „ Mahendra Chamanlal Parekh	3,616	7/128	20
6. „ Surendra Mangaldas Parekh	7,053	14/128	274
7. „ Indrajit Chamanlal Parekh	3,616	7/128	20
	<u>35,469</u>		<u>880</u>

Category 'B':

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Shares held by the partners of the Managing Agents of the firm excluding the holding of the Directors who are also partners as shown above.	Holding of Ordinary shares	Share in the partnership of Mg. Agents' firm	Holding of the 1st Pref. Shares.	
1. Shri Harshavadan Mangaldas	11,053	14/128	274	
2. Mrs. Savitagavri Chamanlal Parekh	3,750	7/128	16	
3. Shri Virendra Chamanlal Parekh	a minor by his mother and guardian Mrs. Savitagavri Chamanlal Parekh.	6,328	7/128	20
4. Shri Manmohan Chamanlal Parekh	-do-	4,462	7/128	20
5. Shri Kamalnayan Chamanlal Parekh	-do-	4,962	7/128	20
6. Shri Nutan Chamanlal Parekh	-do-	4,962	7/128	20
7. Shri Hussein Essa		6,142	8/128	Nil
		<u>41,659</u>		<u>370</u>

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Category 'C':

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Shares represented by the Directors	Holding of ordinary shares	Prof. Shares Holding of the Ist.
1. Sheth Madhusudan Chamanlal Parekh (No. 4 in 'A' above) as Karta of the Joint Family estate of Sheth Chamanlal Girdhardas Parekh	3,899	937
2. Sheth Mathuradas Mangaldas Parekh (No. 2 in 'A' above) as guardian and father of minor, Ben Purnima Mathuradas	1,000	
3. -do- -do- Ben Veena	1,000	
4. -do- -do- Ben Sunita	1,000	
5. -do- -do- Jagatkumar Mathuradas	1,000	
6. Sheth Surendra Mangaldas Parekh (No. 6 in 'A' above) As guardian and father of minor Darshan Surendra Parekh	1,000	
7. -do- as guardian and father of minor Ben Babi Surendra Parekh	1,000	
	9,899	937

It appears that in the past the assessee company incurred heavy losses and it had to reconstruct its capital in 1930 because it had a debit balance of Rs.12,75,000 in the Profit and Loss Account which had to be paid out of capital. This was done by reducing the face value of the Ordinary Shares from Rs. 100 to Rs. 10 each and of the Preference Shares from Rs. 100 to Rs. 25 each, after obtaining the approval of the High

Court. It is the reconstituted capital which has been shown by us in an earlier part of this judgment. It also appears that Income Tax Officer granted to the assessee company a rebate of one anna under proviso (a) to paragraph (B) of part (I) of the Second Schedule of the Finance Act, 1948. This rebate was granted to those companies to which the provisions of s. 23 A were not applicable. Subsequently, the Income Tax Officer, as stated already, applied s. 23 A to this company and it was contended that he was incompetent to do so as he must be deemed to have impliedly held already that s. 23 A was not applicable. Section 23 A before its amendment in 1955, in so far as it is material read as follows:—

“23A. *Power to assess individual members of certain companies.*—(1) Where the Income-tax Officer is satisfied that in respect of any previous year the profits and gains distributed as dividends by any company up to the end of the sixth month after its accounts for that previous year are laid before the company in general meeting are less than sixty per cent of the assessable income of the company of that previous year, as reduced by the amount of income-tax and super-tax payable by the company in respect thereof he shall, unless he is satisfied that having regard to losses incurred by the company in earlier years or to the smallness of the profit made, the payment of a dividend or a larger dividend than that declared would be unreasonable, make with the previous approval of the Inspecting Assistant Commissioner an order in writing that the undistributed portion of the assessable income of the company of that previous year as computed for income-tax purposes and reduced by the amount of income-tax and super-tax payable by the company in respect thereof shall be deemed to have been distributed as dividends amongst the shareholders as at the date of the general meeting aforesaid, and

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thereupon the proportionate share thereof of each shareholder shall be included in the total income of such shareholder for the purpose of assessing his total income:

x	x	x	x
x	x	x	x

Provided further that this sub-section shall not apply to any company in which the public are substantially interested or to a subsidiary company of such a company if the whole of the share capital of such subsidiary company is held by the parent company or by the nominees thereof.

Explanation. — For the purpose of this sub-section,—

a company shall be deemed to be a company in which the public are substantially interested if shares of the company (not being shares entitled to a fixed rate of dividend, whether with or without a further right to participate in profits) carrying not less than twenty-five per cent of the voting power have been allotted unconditionally to, or acquired unconditionally by, and are at the end of the previous year beneficially held by the public (not including a company to which the provisions of this sub-section apply), and if any such shares have in the course of such previous year been the subject of dealings in any stock exchange in the taxable territories or are in fact freely transferable by the holders to other members of the public.”

We are really concerned with the application of the Explanation to the facts of this case. The Explanation, is so far as it is relevant to our purpose, says that a company shall be deemed to be a company in which the public are substantially interested if the

shares of the company carrying not less than 25% of the voting power have been allotted unconditionally to or acquired unconditionally by the public and are held beneficially by the public.

The Income-tax Officer held that this was not a company in which the public were substantially interested and that the grant of the rebate earlier by him did not estop him from applying s. 23A to this company. His order was upheld by the Appellate Assistant Commissioner and the Tribunal on both the points. The assessee company then applied for a reference and the Tribunal referred the following questions for decision by the High Court:--

- “(1) Whether, on the facts and in the circumstances of the case, the Income-tax Officer was competent to pass an order under Section 23A(1) of the Act after having allowed a rebate of one anna per rupee in the assessment under the proviso (a) to paragraph (B) of Part I of the Second Schedule of the Finance Act, 1948?
- (2) If the answer to question No. 1 is in the affirmative whether on the facts and in the circumstances of the case, the assessee company is a company in which the public are substantially interested for the purposes of Section 23A of the Act?
- (3) Whether the loss of Rs. 12,75,000 incurred by the company prior to its reconstruction in 1930, could be taken into consideration for purposes of the applicability of Section 23A (1) of the Act?”

The High Court, by the judgment under appeal, answered the first two questions in the affirmative and in view of the answer to Question No. 2 it considered it unnecessary to answer the third. The Commissioner of Income Tax obtained a certificate of fitness and filed the present appeal.

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The answer to the first question is in favour of the Commissioner of Income Tax. The other side has not appealed and Mr. Vishwanath Sastri for the assessee company conceded before us that the High Court was right. The third question depends on the answer to the first question but as it has not been answered by the High Court we do not consider it necessary to answer it here for the first time. We shall now address ourselves to the second question.

The Tribunal in dealing with the question whether the public could be said to hold 25% or more of the voting power in the assessee company took into consideration a decision of the Privy Council in *Commissioner of Income Tax v. H. Bjordal*,⁽¹⁾ and held that though directors, *qua* directors, do not cease to be members of the public, the holding of the group of 14 individuals who collectively formed the Managing Agency firm of Mangaldas Mehta & Co. could not be counted as held by the members of the public in this case for purposes of the Explanation. The Tribunal was further of the opinion that this group of persons had a 'juristic personality' and it should be taken into account as a group in determining where the Controlling power vested according to the test laid down by the Privy Council in the said case.

The High Court reversed the decision of the Tribunal following its earlier decision reported in *Raghubanshi Mills Ltd. v. Commissioner of Income-Tax*⁽²⁾. In that case the High Court had held that directors, *qua* directors must be contrasted with the public and if the directors held more than 75% of the voting power then alone the company could be said to be one in which the public were not substantially interested. The High Court's view was that the Managing Agents act under the direction of the directors and unless the directors were themselves controlling the voting power above the limit stated by the Explanation, the company must be regarded as one in which

(1) [1955] 28 I. T. R. 25.

(2) [1953] 24 I. T. R. 338.

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the public were substantially interested. Applying the same test to the present case, the High Court found that the directors between them held only the shares which we have shown in tabular form under category 'A'. Since the number of these shares was not up to the mark to attract s. 23A, the High Court answered the second question in favour of the assessee company. The request of the Department that a supplemental statement of the case be asked from the Tribunal as to whether any person belonging to categories 'B' and 'C' was so much within the control of the directors as not to hold the shares unconditionally or beneficially for himself was rejected by the High Court observing that this would give a second chance to the Department to lead further evidence. Following the decision of the House of Lords in *Thomas Fattorini (Lancashire) Ltd. v. Inland Revenue Commissioner*,⁽¹⁾ they refused to take action under s. 66 (4). The High Court took notice of the fact that the Privy Council in *Bjordal's case* (*supra*) had indicated a test to determine what is meant by "public" which was different from that indicated by them in *Raghuvanshi Mill's case* (*supra*). They, however, held that after 1950 the decisions of the Privy Council had only a persuasive authority and the decision of the High Court was binding in the absence of a decision by this Court. They, therefore, applied their own decision in *Raghuvanshi Mill's case* and decided this case accordingly.

It may be pointed out that the High Court did appreciate the point of view expressed by the Privy Council in the above-mentioned case. They observed as follows:—

"It may be that our view is erroneous; and it may be—and very probably it is—that the view taken by the Privy Council is the right one. But, as we have said, so long as the judgment of the Bombay High Court stands, it was the duty both of the Department and of the Tribunal to give effect to that decision."

(1) [1942] A. C. 643.

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Section 23A is not applicable to a company in which the public are substantially interested. What is "substantial" interest of the public is stated in the Explanation. That interest represented in terms of the share-holding must not be less than 25% of the total number of the shares, but no person can be said to belong to the "public" unless he holds the shares unconditionally and beneficially for himself. What is meant by "unconditionally" and "beneficially" was explained by this Court in an appeal against the decision of the High Court of Bombay in the *Raghuvanshi Mills' case*. The decision of this Court is reported in [1961] 41 I.T.R., 613. This Court pointed out that by the words "unconditionally" and "beneficially" is indicated that the voting power arising from the holding of those shares should be free and not within the control of some other shareholder and the registered holder should not be a nominee of another. It was pointed out again by this Court in *Shri Chungdeo Sugar Mills Ltd. v. Commissioner of Income Tax Bombay*,⁽¹⁾ that by "unconditional" and "beneficial" holding is meant that the shares are held by the holders for their own benefit only and without any control of another.

This Court approved the decision of the Privy Council in *Bjordan's case* that directors, *qua* directors, are not without the pale of the public. This Court pointed out that what one has to find out is whether there is an individual who, or a group acting in concert which, controls or control the affairs of the company to the exclusion of others by reason of his or their voting power. Such person or group of persons do not answer the description "public." There is nothing inherent in the office of directors which would lead one to think that the directors must act in unison. They are persons in whom the shareholders have reposed confidence and on whom they have conferred powers which under the scheme of the Companies Act, have to be exercised for the benefit

(1) [1961] 41 I. T. R. 667.

of the shareholders. The directors are, in a manner of speaking, trustees of these powers. It is the duty of the directors to exercise these powers to the best of their independent judgment. There is therefore, nothing in the nature of things or at all that requires the directors to act in unison. This Court pointed out in the *Raghuramshi Mills' case* (1) that such a group may be composed of directors or their nominees or relations in different combinations or may be composed of persons none of whom is a director provided such a group forms a block which holds the controlling interest in its hands.

It would, therefore, follow from what we have stated that we have first to see whether there is an individual or a group holding the controlling interest which group acting in concert can direct the affairs of the company at its will. The controlling interest, of course, is effective only if the group owns 51% of the total shares. But the company will still be a company in which the public can be said to be substantially interested because to cease to be so the shareholding of the group must be more than 75%. In the group, any person, be he a director or a non-director, a relative of a director, a promoter of the company, or a stranger, may be included but only if belonging to a group or as holding the shares as a nominee of someone else belonging to the group. We have indicated again the true test which was not applied in the judgment of the Bombay High Court in the *Raghuramshi Mills' case* (2) and applying which we reversed that decision.

Applying the above test, we have to see whether there is such a group in this company. It is obvious from what we have said that category 'A' which consisted of the directors could not be regarded as outside "public" merely by reason that they were directors. But there is, however, an intimate connection between category 'A' and category 'B' in as much as both are members of the Managing Agency

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(1) [1961] 41 I. T. R. 613.

(2) [1953] 24 I. T. R. 333.

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firm. In other words, there is evidence of yet another group, namely, the group of shareholders who constitute the Managing Agency firm.

We agree with the High Court that Managing Agents act under the control and direction of the directors. The Managing Agents are also appointed by the company. The control of the affairs of a company is ordinarily in the hand of the directors of the company but there may be cases in which the Managing Agents, by reason of their superior holding of shares, may be able to appoint the directors and generally to control the views of the directors. Where the Managing Agents hold an interest which is small and is thus not capable of exercising an overriding power, other evidence may be required to show that they, in conjunction with others, are running the affairs of the company to the exclusion of the public. Where, however, the Managing Agents admittedly hold 51% or more of the shares, it is obvious that the controlling interest belongs to the Managing Agents. When, therefore, the Managing Agents, either by themselves or with those who act in concert with them, hold shares above the 75% limit they can be regarded as constituting a group which cannot be counted as "public". In such a case the holding of the Managing Agents, if above 75%, may furnish proof that the company is one in which the public are not substantially interested. It was contended before us that even among the Managing Agents some may take an independent view. Normally Managing Agencies are not formed by parties except for the purpose of mutual gain and the commonness of the interest lends a cohesion to the body which enables it to act in its own interest. When such a body holds shares carrying more than 75% of the voting power the company itself is run mainly as the Managing Agents desire it to be run. Such a Managing Agency could easily choose its own directors and the directors would not be independent persons but mere nominees of the

Managing Agents. In such a case the inference is irresistible that we have a group, which as a group, can run the company at its will and which not only controls the voting at the meeting of the shareholders but, by selecting its own directors, gets the directors to act according to its own desires. No member of such a Managing Agency firm can be regarded as belonging to "the public" and when this happens the company comes within the reach of s. 23A.

Applying the above test to the present case, it is clear that the Managing Agents, between them hold 77,128 out of 1,00,000 ordinary shares, well above the limit. They have in addition 1,250 First Preference Shares out of 5,000 which also carry voting power. To this must be added 75 shares held by Girdhardas & Co. Ltd. to which s. 23A is admittedly applicable. This brings the total holding to 78,453. 75% of the total shares bearing votes is 78,750. This shows that the holding of the Managing Agents is short by 298 shares for the application of the Explanation to s. 23A. But when we turn to category "C" we find that 6,000 shares were held by the members of the Managing Agency on behalf of minor children and the voting power arising from these shares was in their own hands as guardians. There is no doubt that in the present case shares carrying more than 75% of the voting power are held by persons who form a group in the sense indicated by this Court in *Raghuvanshi Mills case* and by us here. The reason is this: Shares carrying more than 75% of the voting power are held by the partners of the managing agency or persons under its control. Now it seems to us that it is to the interest of the partners of this firm to exercise their voting power in one way, namely the way that brings to them the largest profit out of the company. It is true that the managing agents are the servants of the company in a manner of speaking and not its masters and also that the object of a firm of managing agents is to carry out certain administrative

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duties concerning the company under the control of the directors of the company. That however is irrelevant and in any case is far from the truth in the present case. Here the partners of the managing agency practically own the company.

At the hearing a point was raised that it has to be proved as a fact that the persons constituting the group which owns shares carrying more than seventy-five percent of the voting power, were acting in unison. The test is not whether they have actually acted in concert but whether the circumstances are such that human experience tells us that it can safely be taken that they must be acting together. It is not necessary to state the kind of evidence that will prove such concerted actings. Each case must necessarily be decided on its own facts. The exclusion of "public" in the manner indicated generally from more than 75% of the shares and the concentration of such a holding in a single person or a group acting in concert is what attracts s. 23 (A).

In our opinion, the High Court was not right in answering the second question in the affirmative. The appeal is allowed. The answer of the High Court is set aside and the question is answered in the negative. The respondent shall pay the costs here and in the High Court.

Appeal allowed.