

COMMISSIONER OF INCOME TAX, WEST BENGAL

v.

M/S. ABDUL RAHIM OSMAN & CO. (INDIA) PRIVATE LIMITED

September 19, 1972

[K. S. HEGDE, P. JAGANMOHAN REDDY AND H. R. KHANNA, JJ.]

Indian Income Tax Act, 1922 (Act 11 of 1922)—Section 23A(1)—Scope of.

The respondent is a private company. The assessment was for the years 1958-59 and 1959-60 of which the accounting year ended on 30th June 1957 and 30th June 1958 respectively. The Company had declared dividend after the 12 months following the accounting year, and hence, the Income Tax Officer subjected the Company to Super Tax in terms of the latter part of S. 23A(1) of the Indian Income Tax Act, 1922, by including the dividends of Rs. 15,000 and Rs. 90,000 declared and paid by the Company in respect of relevant accounting years.

The respondent contended that once dividend is declared before an order is made under S. 23-A(1), no Super-Tax can be levied in respect of those dividends. This submission was rejected by the I.T.O., who sought to assess the respondent by including the dividends already declared and paid. An appeal to the Appellate Assistant Commissioner, was unsuccessful. The Tribunal, however, referred the following question to the High Court under S.66(1) of the Indian Income Tax Act 1922: "whether, on the facts of the case, the Tribunal was right in holding that in the matter of calculation of undistributed balance of the total income of an assessee for the purpose of levy of Super Tax, in terms of S.23-A(1) of the Income-tax Act, 1922, the I.T.O. should take into consideration dividend declared by the Company after the period of twelve months immediately following the expiry of the previous years relevant to the assessment years, 1958-59 and 1959-60, but before the date on which the orders under S.23-A(1) had been made by the Income Tax Officer;". The High Court has answered that question in the affirmative and against the Department. The question before this Court was whether the High Court was right in answering the question in the affirmative referred to by the Tribunal. Dismissing the appeal,

HELD: (i) S.23-A(1) has been enacted with a view to deter private Companies which do not distribute more than 60% of their assessable income; otherwise their undistributed balance of the net income will be subjected to additional Super Tax. The object of the Section is to prevent the share-holders in adopting device to avoid payment of Super Tax inasmuch as the rates of Super Tax for the Companies being lower, there may be temptation to get the Company accumulate profits and capitalise them, such as, for instance, to issue bonus shares, which were not assessable as income in the hands of the shareholders. It is done to avoid these artifices and force such companies to declare the minimum statutory dividends. In cases where the provisions have not been complied with, the I.T.O., with the previous approval of the inspecting Assistant Commissioner, may make an order if at the time of the passing of the order, it is found that the company has not distributed its dividends within 12 months immediately following the accounting year less than the statutory percentage of its total income of the accounting year as reduced by the amount of taxes payable by the company. Though the I.T.O. has jurisdiction to pass an order under Sub-Section (1), he has to make a regular assessment of the company under S. 23, which he cannot do if in fact, a

A dividend had been declared before the making of that order, as otherwise, the company's undistributed balance which is assessed by the I.T.O. would exceed its commercial profits.

There is also a likelihood of double taxation because not only the company is charged Super-Tax for not distributing the dividends, but also it will be assessed on the dividends it has in fact distributed, to income tax and once again, to the Super-Tax. Such a result was not intended as the company can declare dividends in General Meetings from the profits earned by it and when that is declared and paid, the I.T.O., though for the nonfulfilment of the conditions prescribed in the Section, may seek to reopen it, he cannot make an assessment in cases where the dividend has actually been declared and paid, before the date of his order. [375F]

CIVIL APPELLATE JURISDICTION : C. A. Nos. 1378 and 1379 of 1969.

C Appeals by certificate from the judgment and order dated May 21, 1968 of the Calcutta High Court in Income-tax Reference No. 17 of 1965.

V. S. Desai, P. L. Juneja, R. N. Sachthey and S. P. Nayar, for the appellants.

D *M. C. Setalvad, S. Roy Chowdhary and G. S. Chatterjee*, for the respondent.

The Judgment of the Court was delivered by

E JAGANMOHAN REDDY, J. This appeal is by certificate and though no reasons have been given for the grant of it, the learned advocate for the respondent does not contest that a question of law does arise and has not objected to the certificate. The question that was referred to the High Court by the Tribunal under s. 66(1) of the Indian Income-tax Act, 1922 (hereinafter called the 'Act') is as follows :—

F “Whether, on the facts and in the circumstances of the case, the Tribunal was right in holding that in the matter of calculation of undistributed balance of the total income of an assessee for the purpose of levy of super-tax in terms of s. 23-A(1) of the Income-tax Act, 1922, the Income-tax Officer should have taken into consideration dividend declared by the company after the period of 12 months immediately following the expiry of the previous years relevant to the assessment years 1958-59 and 1959-60 but before the date on which the orders under s. 23-A(1) had been made by the Income-tax Officer ?

H The High Court has answered that question in the affirmative and against the department following the reasoning which was *obiter* in the case of *Moore Avenue Properties Private Ltd. v. C.I.T.*(¹).

The respondent is a private company to which it is not disputed, sub-s.(1) of s.23-A would be attracted if it fulfilled the conditions prescribed therein. The assessment relating to which the Income-tax Officer sought to exercise his jurisdiction under that section was for the years 1958-59 and 1959-60 for which the accounting year ended on 30th June 1957 and 30th June 1958 respectively. The order of the Income-tax Officer was dated October 31, 1961. The contention of the appellant is that the company had declared the dividends after the 12 months following the accounting year and hence the Income-tax Officer had, with the previous sanction of the Inspecting Assistant Commissioner, validly subjected the company to super-tax in terms of the latter part of s. 23-A(1). On behalf of the respondent it was submitted that once dividends were declared before an order is made under this section no super-tax can be levied in respect of those dividends. This submission was rejected by the Income-tax Officer who sought to assess the respondent by including Rs. 15,000 and Rs. 90,000/- declared as dividends at the general meetings held on December 17, 1959 and May 26, 1960 in respect of the relevant assessment years. An appeal to the Appellate Assistant Commissioner was unsuccessful. The Tribunal however on a reading of the relevant parts of the section came to the conclusion that in computing the undistributed balance of the total income not only the income-tax and super-tax payable by the company but also any other tax levied by the local authority etc. are to be deducted but also "dividends actually distributed, if any" which are the words used in the latter part of s. 23-A(1). It was also of the view that no time limit was applicable in taking into account the actual distribution of dividends in passing an order under s. 23-A(1) by the Income-tax Officer as such it directed that the sums of Rs. 15,000 and 90,000/- were to be taken into account in arriving at the undistributed balance of the total income of the respondent company for the purpose of levy of super-tax. Before considering the contention on behalf of the revenue it will be necessary to examine the terms of the section and the object for which it was enacted. S.23-A(1) after it was re-cast by the Finance Act of 1955 is as follows :—

"Where the Income-tax Officer is satisfied that in respect of any previous year the profits and gains distributed as dividends by any company within the twelve months immediately following the expiry of that previous year are less than the statutory percentage of the total income of the company of that previous year as reduced by—

(a) the amount of income-tax and super-tax payable by the company in respect of its total income, but ex-

A cluding the amount of any super-tax payable under this section;

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

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

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the Income-tax Officer shall, unless he is satisfied that, having regard to the losses incurred by the company in earlier years or to the smallness of the profits made in the previous year, the payment of a dividend or a larger dividend than that declared would be unreasonable, make an order in writing that the company shall, apart from the sum determined as payable by it on the basis of the assessment under section 23, be liable to pay super-tax at the rate of fifty per cent in the case of a company whose business consists wholly or mainly in the dealing in or holding of investments, and at the rate of thirty-seven per cent in the case of any other company on the undistributed balance of the total income of the previous year, that is to say, on the total amount as reduced by the amounts, if any, referred to in clause (a), clause (b) or clause (c) and the dividends actually distributed, if any."

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This provision is procedural and applies only to companies in which the public are not substantially interested. It seems to have been enacted with a view to deter private companies which do not distribute more than 60% of their assessable income on pain of exposing them to the drastic consequences of subjecting their undistributed balance of the net income to additional super-tax. The object of the section is to prevent the shareholders in adopting a device to avoid payment of super-tax inasmuch as the rates of super-tax for the companies being lower there may be a temptation to get the company to accumulate profits and capitalise them such as for instance to issue bonus shares which were not assessable as income in the hands of the shareholders. It is to avoid these artifices and force such companies to declare the minimum statutory dividends, though in the light of the changed definition of 'dividend' under s. 2(6A) profits may attract tax even when they reach the shareholder in capitalised forms, or where they are distributed to them on liquidation from accumulated profits over the years they will be chargeable as dividends.

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In cases where the provisions have not been complied with, the Income-tax Officer with the previous approval and consent of the Inspecting Assistant Commissioner will get jurisdiction to make

an order if at the time of the passing of the order it is found that the company has not distributed by way of dividends within twelve months immediately following the accounting year less than the statutory percentage of its total income of the accounting year as reduced by the amount of taxes payable by the company and in the case of banking companies the amount actually carried to a reserve fund under a statutory compulsion. Though the Income-tax Officer has jurisdiction to pass an order under sub-s.(1) he has to make a regular assessment on the company under s. 23 which he cannot do if in fact a dividend had been declared before the making of that order, as otherwise the company's undistributed balance which is assessed by the Income-tax Officer would exceed its commercial profits. There is also a likelihood of double taxation because not only the company is charged with super-tax for not distributing the dividends, but also it will be assessed on the dividends it has in fact distributed to income-tax and once again super-tax. Such a result was not intended. As the company can only declare dividends in general meeting from the profits earned by it, and when that is declared and paid the Income-tax Officer though for the non-fulfilment of the conditions prescribed in the section may seek to re-open it he cannot make an assessment in cases where the dividend has actually been declared and paid before the date of his order. In this view, we think the High Court was right in answering the question in the affirmative. The appeal is accordingly dismissed with costs.

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Appeal dismissed.