1960

Commissioner of Income-Tax, Bombay
v.
Chandulal Keshavlal & Co.

Kapur J.

not in terms, negativing the Crown's contention. I think that there was ample material to support the findings of the Commissioners, and accordingly that this prohibition does not apply."

Thus in cases like the present one in order to justify deduction the sum must be given up for reasons of commercial expediency; it may be voluntary, but so long as it is incurred for the assessee's benefit the deduction would be claimable.

The Income-tax Appellate Tribunal has found in favour of the Managing Agent that the amount was expended for reasons of commercial expediency, it was not given as a bounty but to strengthen the Managed Company and if the financial position of the Managed Company became strong the Managing Agent would benefit thereby. That finding is one of fact. On that finding the Income-tax Appellate Tribunal rightly came to the conclusion that it was a deductible expense under s. 10(2)(xv).

In our opinion the judgment of the High Court was right and we would dismiss this appeal with costs.

Appeal dismissed.

THE COMMISSIONER OF INCOME-TAX, BOMBAY NORTH & OTHERS.

v.

M/S. HARIVALLABHDAS KALIDAS AND CO.,

1960

February, 19

(S. K. DAS, J. L. KAPUR AND M. HIDAYATULLAH. JJ.)

Income-tax—Managing Agent's Commission payable at the end of the year—Rate of Commission reduced before then by agreement—If voluntary relinquishment of a portion of accrued commission.

The respondent-firm Harivallabhdas Kalidas was appointed the Managing Agent of Shri Ambika Mills Ltd., the appellant in the connected appeal by means of a Managing Agency Agreement the relevant portion of which ran thus:—

"(2)(a) The Company shall pay each year to the said Firm either the commission of 5 (five) per cent on the total sale proceeds of yarn, and of all cloth, manufactured from cotton,

silk, jute, wool, waste and other fibres and sold by the company, or a commission of three pies per pound avoirdupois on the sale, whichever the said Firm choose to take, and also a commission of 10 (ten) per cent on the proceeds of sale of all other materials sold by the Company and 10 (ten) per cent on the bills of any ginning and pressing factories and on any other work done by the Company."

And by clause (5) it was provided:

"(5) The remuneration payable to the said Firm under clause 2(a) shall be paid to the said Firm forthwith after the 31st day of December or such other date as the Directors may fix for the closing of the accounts of the Company in each year and after such accounts are passed by the company in General Meeting."

Subsequently, at the request of the Managed Company the Managing Agents agreed to charge commission at 3 per cent on sales instead of 5 per cent for the year ending December 31, 1950 and a resolution to that effect was passed by the Managed Company and a formal agreement to that effect was executed. The Income-tax Authorities, however, taxed the Managing Agents for two assessment years on the basis that by entering into an agreement with the mills they had voluntarily relinquished certain sums of money as their commission which had accrued to them as income for the purpose of income-tax. An appeal was taken to the Income-tax Tribunal which held that the agreement between the Managing Agent and the Managed Company to receive remuneration at 3 per cent on the total sale was valid and took effect from January, 1, 1950, and the questions whether the commission accrued on the proceeds of every single sale or only when the assessee firm exercised its option to charge it on the total sale proceeds or on the weight of the yarn sold and whether the Managing Agents would get their commission after the whole profit was determined at the end of the year, were decided in favour of the Managing Agents. The High Court also on a reference made to it at the instance of the Commissioner of Income-tax, answered the abovementioned question in favour of the Managing Agents. On appeal by the Income-tax Commissioner by special leave,

Held, that on a proper construction of the agreement, it was clear that there was no accrual of commission till the end of the year and that it did not accrue as and when the sales took place. The Managing Agents were to be paid at the end of the year and by agreeing to the modification of the agreement before then they had not voluntarily relinquished any portion of the commission.

Commissioner of Income-tax, Madras, v. *K.R.M.T.T. Thiagaraja Chetty and Co.*, [1954] S.C.R. 258, *E.D. Sasoon and Co. Ltd.* v. *The Commissioner of Income-tax Bombay City*, [1955] 1 S.C.R. 313 and *Commissioner of Inland Revenue* v. *Gardner Mountain and D' Ambrumenil Ltd.*, 29 T.C. 69, not applicable.

1960

Commissioner of Income-tax, Bombay North
v.
M/s. Harivallabhdas Kalidas

CIVIL APPELLATE JURISDICTION: Civil Appeals Nos. 145/58 and 323/57.

Appeals by special leave from the judgment and order dated September 14, 1955, of the Bombay High Court in I.T. References, Nos. 8 and 21 of 1955 respectively.

R. Ganapathi Iyer and *D. Gupta,* for the appellant in C.A. No. 145 of 1958, and respondent in C. A. No. 323 of 1957.

N. A. Palkhivala, S. N. Andley, J. B. Dadachanji and *Rameshwar Nath,* for the respondent in C. A. No. 145 of 1958 and appellant in C. A. No. 323 of 1957.

1960. February, 19. The Judgment of the Court was delivered by

Kapur J.

KAPUR, J.—This judgment will dispose of two appeals, C. A. No. 145/58 and C. A. 323/57. They arise out of the same transaction i.e. Managing Agency Agreement and the result of C. A. No. 323/57 is dependent upon the judgment in C. A. 145/58 and we propose to deal with the latter appeal which was argued before us and the former for reasons to be stated later was not pressed. The appellant in C. A. 145/58 is the Commissioner of Income-tax, Bombay and the respondent is the assessee, a registered firm, which on March 8, 1941, was appointed the Managing Agents of Shri Ambica Mills Limited (hereinafter termed the Managed Company) the appellant in C. A. 323/57. The duration of the Managing Agency period was 20 years. By clause (2) of the Managing Agency Agreement it was provided:—

"(2)(a) The Company shall pay each year to the said Firm either the commission of 5 (five) per cent. on the total sale proceeds of yarn, and of all cloth, manufactured from cotton, silk, jute, wool waste and other fibres and sold by the company, or a commission of three pies per pound avoirdupois on the sale, whichever the said Firm choose to take, and also a commission of 10 (ten) per cent. on the proceeds of sale of all other materials sold by the Company and 10 (ten) per cent. on the bills of any ginning and pressing factories and on any other work done by the Company.

(b) If in any year the net profits of the Company shall not be sufficient to enable the Directors, if they think fit, to recommend a dividend of eight per cent. per annum on the capital paid up on the ordinary shares for the time being, the same Firm shall be bound to give up from the total amount of commission payable under clause 2(a) hereof such portion thereof as may be necessary to make up the deficit. PROVIDED THAT in no event the amount so given up by the said Firm shall exceed one-third of such total amount of commission".

And by Clause (5) it was provided:

"(5) The remuneration payable to the said Firm under Clause 2(a) shall be paid to the said Firm forthwith after the 31st day of December or such other date as the Directors may fix for the closing of the accounts of the Company in each year and after such accounts are passed by the Company in General Meeting".

On December 9, 1950, the Board of Directors of the Managed Company passed a resolution to the effect that the Directors had for some time past been discussing with the Managing Agents the advisability of modifying the terms of the Managing Agency Agreement as to the commission payable under it and that the Managing Agents had agreed to charge 3 per cent. on sales instead of 5 per cent. for the year ending December 31, 1950. A resolution was passed at the Annual General Meeting of the Managed Company on April 22, 1951, which was to the same effect. The resolution of the Board of Directors was ratified at an Extraordinary General Meeting of the shareholders of the Managed Company on October 7, 1951, and the same day a formal agreement embodying the terms of the resolution was executed between the Managing Agents and the Managed Company. For the accounting years 1950 and 1951 i.e. assessment years 1951-52 and 1952-53 the Managing Agents were taxed by the Income-tax Authorities on the basis that in those two years they had voluntarily relinquished a sum of Rs. 1,69,981 and Rs. 2,10, 530 for the respective assessment years. These sums were added to the income of the Managing Agents for the purpose of income-tax.

1960

Commissioner of Income-tax, Bombay North
v.
M/s. Harivallabhdas Kalidas

Kapur J.

An appeal was then taken to the Income-tax Appellate Tribunal and it was held by the Tribunal that the agreement between the Managing Agents and the Managed Company to receive remuneration at 3% on the total sales was a valid one and took effect as from January 1, 1950. The second question, whether the commission accrued on the proceeds of every single sale or it accrued only when the assessee firm exercised its option to charge its commission on the total sale proceeds or on the weight of the yarn sold and whether the Managing Agents were to get the amount of commission after the whole profit was determined at the end of the year, was decided in favour of the Managing Agents. A Reference was made to the High Court at the instance of the Commissioner of Income-tax and the questions abovementioned were answered in favour of the Managing Agents. This appeal by the appellant has been brought against the judgment of the High Court by special leave.

In the connected appeal i.e. C. A. 323/57 by the Managed Company the facts are the same except that the Appellate Tribunal allowed the Managed Company the sum on which the Managing Agents were to be taxed as allowable deduction. When the Commissioner got the case stated to the High Court the Managing Company also had a case stated. But as the High Court upheld the contention of the Managing Agents the Managed Company did not press its application which was therefore dismissed. The appeal of the Managed Company is brought against that order.

In the appeal by the Commissioner of Income-tax, i.e. C. A. 145/58, it was argued that according to the terms of the Agency Agreement the Managing Agents were to get the commission on the sales and as the accounts were kept on a mercantile basis, the amount of commission accrued as and when the sales took place and paragraph 5 of agreement was only a machinery for quantifying the amount. It was also argued that the Managing Agents by entering into an agreement with the Mills had voluntarily relinquished a portion of the amount of commission which had accrued to them and therefore the whole of the income from commission which had already accrued was liable to

income-tax; and reference was made to the cases reported as *Commissioner of Income-tax, Madras* v. *K. R. M. T. T. Thiagaraja Chetty and Co.* (1), *E. D. Sassoon & Company Ltd.* v. *The Commissioner of Income-tax, Bombay City* (2) and to an English case *Commissioners of Inland Revenue* v. *Gardner Mountain & D' Ambrumenil Ltd.* (3). But these cases have no application to the facts of the present case. In the *Commissioner of Income-tax, Madras* v. *K. R. M. T. T. Thiagaraja Chetty & Co.* (1), the assessee firm was, under the terms of the Managing Agency Agreement, entitled to a certain percentage of profits and in the books of the Company a certain sum was shown as commission due to the assessee firm and that sum was also adopted as an item of business expenditure and credited to the Managing Agents' commission account but subsequently it was carried to suspense account by a resolution of the Company passed at the request of the assessee firm in order that the debt due by the Firm might be written off. The accounts were kept on mercantile basis and it was held that on that basis the commission accrued to the assessee when the commission was credited to the assessee's account and subsequent dealing with it would not affect the liability of the assessee to income-tax. It was also held that the quantification of the commission could not affect the question as it was not a condition precedent to the accrual of the commission. At page 267 Ghulam Hassan J., observed:—

"Lastly it was urged that the commission could not be said to have accrued, as the profit of the business could be computed only after the 31st March, and therefore the commission could not be subject to tax when it is no more than a mere right to receive. This argument involves the fallacy that profits do not accrue unless and until they are actually computed. The computation of the profits whenever it may take place cannot possibly be allowed to suspend their accrual. In the case of income where there is a condition that the commission will not be payable until the expiry of a definite period or the making up of the account, it might be

(1) [1954] S.C.R. 258 at 267. (2) [1955] 1 S.C.R. 313, 344.
(3) 29 T.C. 69, 96.

1960

Commissioner of Income-tax, Bombay North
v.
M/s. Harivallabhdas Kalidas

Kapur J.

said with some justification, though we do not decide it, that the income has not accrued but there is no such condition in the present case".

This passage does not help the appellant's case. The question there decided was that the accrual of the commission was not dependent upon the computation of the profits although the question whether it would make any difference where the commission was so payable or was payable after the expiry of a definite period for the making of the account was left undecided. In the case before us the agreement is of a different nature and the above observations are not applicable to the facts of the present case.

The next case is *E. D. Sassoon & Co., Ltd.* v. *The Commissioner of Income-tax, Bombay City* (1). But it is difficult to see how it helps the case of the appellant. If anything it goes against his contention. In that case the assessee Company was the Managing Agent of several Companies and was entitled to receive remuneration calculated on each year's profits. Before the end of the year it assigned its rights to another person and received from him a proportionate share of the commission for the portion of the year during which it worked as Managing Agent. On the construction of the Managing Agency Contract it was held that unless and until the Managing Agent had carried out one year's completed service, which was a condition precedent to its being entitled to receive any remuneration or commission it was not entitled to receive any commission. The facts in that case were different and the question for decision was whether the contract of service was such that the commission was only payable if the service was for a completed year or the assessee Company was entitled to receive even for a portion of the year for which it had acted as a Managing Agent. It was held that it was the former.

As was observed by Lord Wright in *Commissioners of Inland Revenue* v. *Gardner, Mountain & D'Ambrumenil Ltd.* (2), "It is on the provisions of the contract that it must be decided, as a question of construction and therefore of law, when the commission was earned". The contract in the present case in para-

(1) [1955] 1 S.C.R. 313, 344. (2) 29 T.C. 69, 96.

1960

Commissioner of Income-tax Bombay North
v.
M/s. Harivallabhdas Kalidas

Kapur J.

graph 2 shows that (1) the company was to pay each year; (2) that the Managing Agents were to be paid 5 per cent. commission on the proceeds of the total sales of yarn and of all cloth sold by the Company or three pies per pound avoirdupois on the sale, whichever the . Managing Agents chose; thus there was an option to be exercised at the end of the year; (3) they were also to be paid at 10 per cent. on the proceeds of sales of all other materials; and (4) the Mills were to pay to the Managing Agents each year after December 31, or such other date which the Directors of the Company may choose for the closing of the accounts. There was a further clause that if the net profits of the Managed Company, that is, the Mills were not sufficient to enable the Directors to recommend a dividend of 8 per cent. per annum on the paid up capital, then the Managing Agents were bound to forego a portion of their commission upto one-third. All these provisions as to payment have to be read together as an indivisible and an integral whole. On a proper construction of this contract, therefore, it is obvious that the Managing Agents were to be paid at the end of the year. They had the option of receiving a percentage on total sales or three pies per pound and this was exercisable at the end of the year. There was also a liability to pay back a portion of the commission in certain contingencies which also could be determined only when the accounts were made up for the year. It is thus clear that there was no accrual of any commission till the end of the year. On this construction of the contract it cannot be held that the commission had accrued as and when the sales took place and that as a result of their agreeing to the modification of the agreement the Managing Agents had voluntarily relinquished a portion of their commission. On the other hand under the original agreement the Managing Agents were entitled to receive commission only at the end of the year and before then the agreement was varied modifying its terms as from the beginning of the accounting year.

We are of the opinion, therefore, that the High Court correctly found against the appellant and we therefore dismiss C. A. No. 145 of 1958 with costs. In

1960

Commissioner of Income-tax, Bombay North
v.
M/s Harivallabhdas Kalidas

Kapur J.

view of this Mr. Palkiwala for the Managed Company did not press C. A. No. 323 of 1957, which is therefore dismissed but the parties will bear their own costs in that case because the result of that appeal is really dependent upon the result in C. A. No. 145 of 1958.

Appeals dismissed

THE BIHAR STATE CO-OPERATIVE BANK LTD.

v.

THE COMMISSIONER OF INCOME-TAX

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

1960

February 22

Income Tax—Co-operative Bank—Interest received on deposits with other banks—Exemption from taxation under Notification—Indian Income-tax Act, 1922 (XI of 1922) ss. 10, 12.

The Appellant Bank which was registered under the Co-operative Societies Act, 1922, received, in the relevant account years, by way of interest on deposits with the Imperial Bank of India certain sums of money. The Income-tax Officer assessed the aforesaid sums under s. 12 of the Indian Income-tax Act 1922, as income from other sources, but the appellant claimed that the deposits were made not with the idea of making investments but for the purpose of carrying on its business as a bank and that as the interest received on the deposits was profit attributable to its business activities it was not subject to income-tax because of the Notification issued by the Central Government under s. 60 of the Act. Under the Notification profits of any Co-operative Society are exempt from the tax payable under the Act but not income derived from "other sources" referred to in s. 12 of the Act.

Held, that the interest from deposits received by the Appellant Bank in the present case arose out of a transaction entered into for the purpose of carrying on its banking business and fell within the income exempted under the Notification.

The Punjab Co-operative Bank Ltd. v. *The Commissioner of Income-tax, Punjab,* [1940] 8 I.T.R. 635, relied on.

CIVIL APPELLATE JURISDICTION: Civil Appeals Nos. 228 to 230 of 1958.

Appeals from the judgment and decree dated July 2, 1957, of the Patna High Court in Misc. Judicial Case No. 640 of 1955.