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of the previous year, and it would not cover something which is not the income of the previous year, or made fictionally so. The Finance Act could have gone further, as pointed out by the learned Chief Justice in the extract quoted, and made the profits a part of the total income of the previous year under assessment, but it did not do so. The Finance Act could have also resorted to some other fiction, which might conceivably have met the case; but it has failed to do so. Even if one considers the dividends as having come out of the profits of preceding years, they do not become the income of the relevant previous year, and unless the Finance Act expressly laid down that it should be taxed as part of the total income, the purpose is not achieved. Indeed, the Finance Act continues to say that the tax shall be on the total income, as defined in the Indian Income-tax Act and as determined under that Act. It is impossible to say that the additional income-tax was properly laid upon the total income, because what was actually taxed was never a part of the total income of the previous year.

For these reasons, we are of opinion that the High Court was right in answering the question which it had framed, in the negative.

In the result, the appeal fails, and is dismissed with costs.

*Appeal dismissed.*

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## THE COMMISSIONER OF INCOME-TAX, BOMBAY

*v.*

## THE JALGAON ELECTRICITY SUPPLY CO., LTD.

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*May 4.*

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

*Additional Income-tax—If could be levied on excess dividends, when there are profits in the preceding years—Manner of calculation of tax—Indian Finance Act, 1949 and 1950, Para. B, of Part I of the First Schedule.*

After making all allowances and deductions, the income of the assessee company was finally assessed for the years 1949-50

and 1950-51 at Rs. 3,423 and Rs. 3,312 respectively. The assessee company had declared dividends of Rs. 46,024 and Rs. 56,326 for the above two years. Though no profits were brought forward from the previous years, the income-tax officer applied the proviso to para. B of Part I of the Third and First Schedules of the Finance Act, 1949 and 1950, assessed the difference in each year to additional income-tax and charged income-tax at the rate of annas 5 in the rupee on the amounts for the two assessment years. The High Court held that though excess dividends were, in fact, paid, the absence of profits from previous years rendered the Finance Act unworkable in this case.

The question was if the second proviso to para. B read with the explanation which sets out the manner of calculation of the tax applied and whether it was the intention of the Finance Act to levy the additional income-tax on the excess dividends even if there were no profits brought forward from preceding year or years :

*Held*, that the second proviso to para. B of Part I of the first schedule of the Finance Act, 1950, which corresponds to the corresponding paragraph of the Finance Act, 1949, introduces a fiction which postulates that there should be undistributed profit of one or more years immediately preceding the previous year, that such undistributed profits should be sufficient to cover the amount of excess dividend actually paid out in the year under assessment, and that the undistributed profits should not have b en taken likewise to cover an excess dividend of any other previous year. The excess dividends have first to be connected with the profits of the preceding years and then the tax borne on those profits has to be found out, and tax is then payable at an enhanced rate and amounts to the difference between the tax actually borne by the profits and that demandable under the paragraph. Where there are no profits of any preceding year or years, the fiction wholly fails and the method of calculation, equally so.

*Held*, further, that the income-tax law seeks to put in the net certain class of income, and can only successfully do so, if it frames a provision appropriate to that end. If the law fails and the taxpayer cannot be brought within its letter, no question of unjustness as such, arises.

CIVIL APPELLATE JURISDICTION : Civil Appeal No. 477 of 1957.

Appeal from the judgment and order dated September 9, 1955, of the Bombay High Court in Income-tax Reference No. 37/x of 1954.

*K. N. Rajagopal Sastri* and *D. Gupta*, for the appellant.

*N. A. Palkhivala, B. K. B. Naidu* and *I. N. Shroff*, for the respondent.

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1960. May 4. The Judgment of the Court was delivered by

HIDAYATULLAH, J.—This appeal is with a certificate granted by the High Court against its judgment and order dated September 9, 1955, in a reference under s. 66(1) of the Indian Income-tax Act. The Tribunal had referred the following questions for the decision of the High Court:

"(1) Whether there was any excess dividend declared by the assessee Company?

(2) Whether the assessee Company is liable to pay additional income-tax in respect of the excess dividend paid by the assessee Company?"

The High Court answered the first question in the affirmative and the second, in the negative. The Commissioner of Income-tax, Bombay is the appellant before us, and the Jalgaon Electric Supply Co., Ltd. (the assessee Company) is the respondent.

The facts of the case are simple. For the assessment years 1949-50 and 1950-51, the book profits of the assessee Company were respectively Rs. 1,22,469 and Rs. 76,886. After adjustment of depreciation allowance and other deductions, the income of the assessee Company was finally assessed at Rs. 3,423 and Rs. 3,312 respectively. The assessee Company declared a dividend of Rs. 46,024 in the first year and Rs. 56,326 in the next. The Income-tax Officer, applying the Proviso to Para. B of Part I of the Third and First Schedules of the Finance Acts, 1949 and 1950 respectively, assessed the difference in each year to additional income-tax, and charged income-tax at the rate of 5 annas in the rupee on the amounts for the two assessment years. The assessee Company appealed first to the Appellate Assistant Commissioner and then to the Tribunal. In the Tribunal, there was a difference of opinion between the President and the Accountant Member, the former holding that the assessee Company was not liable and the latter, that it was. The case was then referred to a third Member, who agreed with the President. The main reason for the decision of the majority was that there were no profits in the years preceding the previous year, and that, therefore, the said Paragraphs could not, on their terms, operate in

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the circumstances. The view of the minority was that even if there were no profits, the intention of the Finance Act to levy the additional income-tax on the excess dividends was perfectly plain, and that the assessee Company was liable. It may be mentioned at this stage that the decision of the Tribunal turned entirely upon the fact that no profits were brought forward from the previous years, and that, therefore, the Paragraphs could not be applied. The High Court held that though excess dividends were, in fact, paid, the absence of profits from previous years rendered the Finance Act unworkable in this case. It, therefore, accepted the reasons given by the Tribunal, and upheld its decision.

Paragraph B of Part I of the First Schedule of the Finance Act, 1950 corresponds to the corresponding Paragraph of the Finance Act, 1949. It is, therefore, not necessary to refer to them separately. We shall confine ourselves to the Finance Act, 1949. It may also be pointed out that the circumstances of the two years are also on par, except that the amounts of income and the excess dividends are different. The paragraph reads as follows:

"B. In the case of every company—

| | Rate |
|---|---|
| On the whole of total income ...... | Five annas in the rupee: |

Provided that in the case of an Indian Company—

(i) where the total income, as reduced by seven annas in the rupee and by the amount, if any, exempt from income-tax, exceeds the amount of any dividends (including dividends payable at a fixed rate) declared in respect of the whole or part of the previous year for the assessment for the year ending on the 31st day of March, 1950, and no order has been made under sub-section (1) of section 23A of the Income-tax Act, a rebate shall be allowed at the rate of one anna per rupee on the amount of such excess;

(ii) where the amount of dividends referred to in clause (i) above exceeds the total income as reduced by seven annas in the rupee and by the amount, if any, exempt from income-tax, there shall be charged

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on the total income an additional income-tax equal to the sum, if any, by which the aggregate amount of income-tax actually borne by such excess (hereinafter referred to as 'the excess dividend') falls short of the amount calculated at the rate of five annas per rupee on the excess dividend.

For the purposes of the above proviso, the expression 'dividend' shall have the meaning assigned to it in clause (6A) of section 2 of the Income-tax Act, but any distribution included in that expression, made during the year ending on the 31st day of March, 1950, shall be deemed to be a dividend declared in respect of the whole or part of the previous year.

For the purpose of clause (ii) of the above proviso, the aggregate amount of income-tax actually borne by the excess dividend shall be determined as follows:—

(i) the excess dividend shall be deemed to be out of the whole or such portion of the undistributed profits of one or more years immediately preceding the previous year as would be just sufficient to cover the amount of the excess dividend and as have not likewise been taken into account to cover an excess dividend of a preceding year;

(ii) such portion of the excess dividend as is deemed to be out of the undistributed profits of each of the said years shall be deemed to have borne tax,—

(a) if an order has been made under sub-section (1) of section 23A of the Income-tax Act, in respect of the undistributed profits of that year, at the rate of five annas in the rupee, and

(b) in respect of any other year, at the rate applicable to the total income of the company for that year reduced by the rate at which rebate, if any, was allowed on the undistributed profits."

The scheme of the Finance Act in relation to excess dividends and their chargeability to additional income-tax has been examined by us in Civil Appeal No. 427 of 1957 decided today. We are concerned in this case with the application of the second Proviso

to the Paragraph, read with the explanations (not so-called), which set out the manner of calculation of the tax. As we have already pointed out in the other case, the additional income-tax is payable if dividends in excess of the limit fixed by the legislature are paid in any year. This additional income-tax takes note of such tax as might have been paid on the profits, albeit at a lower rate, in any previous assessment year and gives deduction for that amount. The additional income-tax is payable on the excess dividends calculated at a different rate but allowing for the tax already paid. For this purpose, the aggregate amount of income-tax to be borne by the excess dividends has to be calculated in a particular manner. This manner is indicated in the Paragraph, and it begins by providing that the excess dividend shall be deemed to be out of the whole or such portion of the undistributed profits of one or more years preceding the previous year as would be just sufficient to cover the amount of the excess dividend and were not likewise taken into account to cover an excess dividend of a previous year. It is then provided that the excess dividends which are so deemed to be the undistributed profits of each of the previous years shall be deemed to have borne the tax.

The fictions which have been introduced postulate that there should be undistributed profits of one or more years immediately preceding the previous year, that such undistributed profits should be sufficient to cover the amount of excess dividend actually paid out in the previous year under assessment, and that the undistributed profits should not have been taken likewise to cover an excess dividend of any other previous year. Where there are no profits of any preceding year or years, the fiction wholly fails and the method of calculation, equally so. We do not agree with the argument of the Commissioner that the fiction can be given effect to, even if the profits of preceding years do not exist. The argument suggests that the chargeability of excess dividends to additional income-tax can arise under the terms of the Paragraph even in such circumstances. But a plain reading of the Proviso clearly shows that the excess

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dividends have first to be connected with the profits of the preceding years and then the tax borne on those profits has to be found out, and the tax is payable at an enhanced rate and amounts to the difference between the tax actually borne by the profits and that demandable under the Paragraph. The High Court repelled the argument of the Commissioner in much the same way as we have done, and we entirely agree with the reasons given by it.

The Accountant Member, whose decision was in a minority, gave two reasons. The first was that " the explanation provides for the determination of the years out of the profits of which the excess dividend has come ", and the second was that " in order to escape the liability imposed by Cl. (ii), the company must prove that the excess dividend has borne tax 5 annas in the rupee as it is only in that event that the additional tax payable will be nil ". These reasons were also put before us for acceptance. We are, however, unable to agree. The fiction cannot be whittled down in the manner suggested in the first reason. The fiction incorporates within itself not only what the Accountant Member says but also a mode of calculation, which is not a part of the fiction. It is the mode of calculation which cannot be given effect to, though we would go further and say that the fiction itself fails because no profits of preceding years at all existed. The second reason given by the Accountant Member assumes the liability to pay tax, and that is not permissible, because that is the fact in issue to be decided. That fact can only be decided if the Paragraph can be made applicable to the present case and not otherwise. We cannot start with the assumption that additional income-tax on excess dividend has got to be paid, whether the Paragraph applies or not. That would be begging the very question to be decided.

The Commissioner also suggested numerous modifications of the language to give effect to the intention to levy additional income-tax on excess dividends, and pointed out, as did the Accountant Member, that it would be unjust to allow an escapement of tax, where there were no profits of preceding years, to set off

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against the excess dividends. In our opinion, the question of modification of the language cannot arise in the circumstances of the case. Our reasons have been given in Civil Appeal No. 427 of 1957, decided today, and we need not go over the ground again. There is also no question of unjustness involved. The Income-tax law seeks to put in the net certain class of income, and can only successfully do so, if it frames a provision appropriate to that end. If the law fails and the tax-payer cannot be brought within its letter, no question of unjustness as such, arises. The answers given by the High Court to the two questions were correct in the circumstances of the case.

In the result, the appeal fails, and will be dismissed with costs.

*Appeal dismissed.*

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## KAVALAPPARA KOTTARATHIL KOCHUNI AND OTHERS

*v.*

## THE STATE OF MADRAS AND OTHERS

1960

May 4.

(B. P. SINHA, C. J., JAFER IMAM, A. K. SARKAR, K. SUBBA RAO and J. C. SHAH, JJ.)

*Marumakkathayam Law—Enactment for removal of doubts—Constitutional validity—Madras Marumakkathayam (Removal of Doubts) Act, 1955 (32 of 1955)—Constitution of India, Arts. 19(1)(f), 31, 31A.*

These petitions by the holder of Kavalappara Sthanam, his wife, daughters and son challenged the constitutional validity of the Madras Marumakkathayam (Removal of Doubts) Act, 1955, passed by the Madras Legislature soon after the Privy Council had declared the properties in possession of the Sthanee to be Sthanam properties in which the members of the tarwad had no interest. Section 2 of the Act, which contained the substantive provision, was as follows:—

"2. Notwithstanding any decision of Court, any sthanam in respect of which:—

(a) there is or had been at any time an intermingling of the properties of the sthanam and the properties of the tarwad, or

(b) the members of the tarwad have been receiving maintenance from the properties purporting to be sthanam properties as of right, or in pursuance of a custom or otherwise, or

(c) there had at any time been a vacancy caused by there being no male member of the tarwad eligible to succeed to the Sthanam,