

Commissioner of Income-tax, Central Bombay Vs. Cotton Agents Limited

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Court : Mumbai

Decided On : Feb-11-1957

Reported in : [1957]31ITR744(Bom)

Judge : Chagla, C.J. and ;Tendolkar, J.

Acts : [Income Tax Act, 1922](#) - Sections 4

Appeal No. : Income-tax Reference No. 53 of 1956

Appellant : Commissioner of Income-tax, Central Bombay

Respondent : Cotton Agents Limited

Advocate for Def. : R.J. Kolah, Adv.

Advocate for Pet/Ap. : Adv. General

Judgement :

Chagla, C.J.

1. Messrs. Shivnarayan Surajmal Nemani were the managing agents of the New Swadeshi Mills of Ahmedabad Ltd. Prior to 1945. On the 4th January, 1945, the managed company passed a resolution approving the transfer of the managing agency to the assessee. Under the agreement arrived at the assessee became entitled to the managing agency commission from the 1st April, 1944. The managing agency commission from the 1st April, 1944, to the 31st December, 1944, amounted to Rs. 2,20,433 and the managing agency commission from 1st January, 1945, to 31st March, 1945, amounted to Rs. 67,959. The year of account of the assessee was 18th October, 1944, to 4th November, 1945, and the contention of the assessee was that for the assessment year 1946-47 they were liable to pay tax only on the commission of Rs. 67,959 which they had earned by working as managing agents of the managed company and they were not liable to pay tax on the sum of Rs. 2,20,433. This contention of the assessee was not accepted by the Taxing Department. The Tribunal decided in favour of the assessee and the Commissioner has now come before us on this reference.

2. The managing agency agreement provides :

'The remuneration of the agents as such agents of the company as aforesaid shall be as follows :

A commission at the rate of three and a half per cent. on the gross proceeds of all

sales of the yarn, cloth, waste and other articles manufactured by the company earned in any year or other period for which the accounts of the company are made up and laid before the general meeting.'

3. There is a further provision in this agreement, viz.,

'The said commission shall become due to the managing agents at the end of each financial year or other period for which the accounts of the company are to be laid before the general meeting and shall be payable and paid immediately after such accounts have been passed by general meeting.'

4. The contention of the assessee is that inasmuch as the commission is payable on sale proceeds, the commission accrued to Messrs. Shivnarayan Surajmal Nemani for the period during which they were the managing agents up to the 31st December, 1944, and that the commission only accrued to the assessees after they were appointed managing agents on the 1st January, 1945, and they are liable to pay tax only for the period 1st January, 1945, to 31st March, 1945. The Advocate-General on behalf of the Commissioner has relied on the recent decision of the Supreme Court of the Commissioner has relied on the recent decision of the Supreme Court reported in *E. D. Sassoon & Co. Ltd., and Others v. Commissioner of Income-tax, Bombay City*, and the whole debate before us has centered round the question as to whether this decision of the Supreme Court applies to the facts of this case or whether this decision is distinguishable.

5. In *E. D. Sassoon & Co. Ltd., and Others v. Commissioner of Income-tax, Bombay City*, the question that arose for the decision of the Supreme Court was whether the managing agency commission could be apportioned between the original managing agents and the managing agents to whom the managing agency had been transferred. The original managing agents had worked for a portion of the time and for the rest of the time the assignee has worked as managing agents. We took the view that the managing agency commission was apportionable and should be apportioned. The Supreme Court rejected that contention. What Mr. Kolah points out is that the ration of this decision rests upon the fact that in *Sassoon's* case the commission was payable on the profits of the managed company and in the case before us commission is payable on sale proceeds, and what Mr. Kolah urges is that the Supreme Court came to the decision which it did because profits cannot be ascertained till the end of the year and the managing agency commission only accrued when the profits accrued, which was at the end of the year, but in our case every sale that takes place has embedded in it the right of the managing agents to receive their commission, and nothing turns on what the state of the profits of the company is at the end of the year; whether the company earns profits or suffers losses, the right of the managing agents to receive commission depends upon a sale taking place, and according to Mr. Kolah the right to receive commission, which is the same as the accrual of the commission, arises on the sale being effected and not on the earning of the profits. There is considerable force in Mr. Kolah's contention, but we find when we look at the judgment of the Supreme Court that the decision is based not merely on the fact that in *Sassoon's* case the commission was payable on profits. If that had been so, undoubtedly we could have distinguished that case and come to a decision in favour of Mr. Kolah. But when we carefully look at the judgment of the Supreme Court, we find that what had been so, undoubtedly we could have distinguished that case and come to a decision in favour of Mr. Kolah. But when we carefully look at the judgment of the Supreme Court, we find that what the Supreme Court has decided is that the

managing agents are entitled to their commission only when a debt is created in their favour. In other words, with respect, the Supreme Court has equated the creation of a debt with the right to receive a certain amount by the managing agents from the managed company. There is great force in Mr. Kolah's argument that there are two distinct stages which have got to be kept in mind; one is the right to receive the payment and the other is when the payment becomes receivable or when a debt is created or when the payment is made enforceable; and what Mr. Kolah strongly urges upon us is that in this case although the debt may be due by the managed company at the end of the year, although the payment to be received by the managing agents May not be enforceable till the end of the year, the right to receive the payment arose when the sales were effected. Mr. Kolah has drawn our attention to certain decisions where this distinction between the right to receive a payment and the payment becoming receivable is borne out. But whatever view we may take of the contention put forward by Mr. Kolah, we are bound by the decision of the Supreme Court, and as we shall presently point out, the Supreme Court, again with very great respect, has not kept this distinction in mind. It may be that the decision of the Supreme Court, with respect, needs elucidation, but that elucidation can only be given by the Supreme Court itself and not by us. We are in duty bound to follow the decision of the Supreme Court and if we are clear in our mind that the Supreme Court has laid down a particular principle and if that principle is deducible from its judgment we must apply that principle to the facts before us.

6. Now, at the bottom of page 51 this is what Mr. Justice Bhagwati has delivered the judgment of the majority :

'But in order that the income can be said to have accrued to or earned by the assessee it is not only necessary that the assessee must have contributed to its accruing or arising by rendering services or otherwise but he must have created a debt in his favour. A debt must have come into existence and he must have acquired a right to receive the payment. Unless his contribution or parenthood is effective in bringing into existence a debt or a right to receive the payment or in other words a debitum in praesenti solvendum in futuro, it cannot be said that any income has accrued to him. The mere expression 'earned' in the sense of rendering the services etc. by itself is of no avail.'

7. Therefore, what is emphasised by Mr. Justice Bhagwati in this passage is that a debt must have come into existence and also he must have acquired a right to receive the debt. It is true that whenever a debt comes into existence there is a right to receive payment, but Mr. Justice Bhagwati has not accepted the converse of this proposition for which Mr. Kolah is contending that there may be a right to receive payment without a debt coming into existence. Attention might also be drawn to another aspect of the decision of the Supreme Court which has considerable bearing on the facts of our case also. The Supreme Court took the view that the managing agents had no right to claim the commission till they had served for the stipulated period, viz., one year, and the rendering of that service for one year was a condition precedent to their right to the commission. This will be clear from the passage at page 37 :

'It was a condition precedent to the Sassoons earning the remuneration that they fulfilled the terms of their employment and completed the period for which the remuneration was payable to them and the service for the particular period was a condition precedent to their earning the remuneration for that period.'

8. Again at page 43 it is stated :

'The commission was thus an annual payment calculated upon the annual net profits of the company and was to be due to the managing agents yearly on the 31st March in each and every year.'

9. Therefore, in this sentence the Supreme Court emphasises three aspects of the agreement, viz., that the commission was an annual payment, that it was payable on the 31st of March in each and every year, and the mode of calculation was that it was to be calculated upon the annual net profits of the company. Later on, on the same page there is a further passage :

'Until and unless the accounting year of the company had gone by the managing agents have served the company as their agents for the full period no part of the managing agency commission which was payable per year in the manner aforesaid could become due to them and the performance of the service for the year was a condition precedent to the managing agents being entitled to any part of the remuneration, or commission for the accounting year of the company. The managing agency agreement therefore was an entire and indivisible contract stipulating a payment of remuneration or commission per year and enjoined upon the managing agents the duty and obligation of rendering the services to the company for the whole year by way of condition precedent to their earning any remuneration or commission for the particular accounting year.'

10. We would like to add that the other aspect of the matter which Mr. Kolah has emphasised also seems to have been present to the mind of the learned Judges of the Supreme Court because at page 50 they cite with approval the observations of Lord Justice Fry in *Colquhoun v. Brooks*, to effect that the words 'accrual' and 'arising' are used in contradistinction to the word 'receive' and indicate a right to receive, and that they represent a state anterior to the point of time when the income becomes receivable and cannot a character of the income which is more or less inchoate. This observation may create some difficulty in view of the clear and emphatic position accepted by Mr. Justice Bhagwati as already pointed out at the bottom of page 51 and the beginning of page 52. This again proves, if we might say so with respect, the necessity for a further elucidation of the matter by the Supreme Court itself.

11. Mr. Kolah has drawn our attention to the fact in the case of the Supreme Court the commission was not payable at the rate of any particular amount, whereas in the case before us it is payable at the rate of 3 1/2 per cent. on the gross proceeds of all sales, and Mr. Kolah has relied on the judgment in *Moriarty v. Regents of Garage and Engineering Co. Ltd.* In that case the Court of Appeal drew a distinction between the fees of the director payable every year and the fees payable at the rate of so many pounds per year, and the decision suggests that if the latter expression is used and if a director serves for a portion of the year his fees could be apportioned. Mr. Kolah wishes to apply the principle of that decision to the facts of this case and he says that although the commission may have accrued at the end of the year in the light of the Supreme Court's decision, inasmuch as it is payable at the rate of 3 1/2 per cent. on the sale proceeds, it is capable of being apportioned and therefore it should be apportioned according to the sales effected while Messrs. Shivnarayan Surajmal Nemani were managing agents and for the period when the assesseees were managing agents. We would have given serious thought to this aspect of the matter but for the view we take that the decision of the Supreme Court with regard to the question of

creation of the debt and with regard to the serving by the managing agents for a term of one year being a condition precedent for their being entitled to receive payment, is indistinguishable on the facts of this case. We may point out that here as in the Sassoon's case the commission of 3 1/2 per cent. is to be earned in any year, and also by clause 3 of the agreement the commission is to become due to the managing agents at the end of each financial year. Therefore, till the end of the financial year there is no debt whatsoever created in favour of the managing agents and also their right to receive payment depends upon their having served for a whole year. Under the circumstances we must hold, following the decision of the Supreme Court, that the assesseees are liable to pay tax on the whole of the commission as the commission accrued due on the 31st March, 1945, and they became entitled to receive it at the end of the year. We do not agree with the view of the Tribunal that according to the agreement of the managing agents the debt was created in favour of the agents when the goods were sold by the company and that the payment was deferred to a date after the accounts having been passed by the shareholders in the general meeting of the company. In no view of the case can it be said that the debt was created in favour of the agents when the goods were sold. The debt was only created at the end of the financial year. All that can be said - and that is what Mr. Kollah has said - was that the right to receive payment arose when the goods were sold, and the Tribunal has not drawn a distinction which Mr. Kollah has drawn between the right to receive payment and the creation of the debt.

12. The result is that we must answer the question submitted to us : 'Accrued to the assesseees.'

13. We might state before parting with this reference that we are told by Mr. Kollah that the Taxing Department has also assessed Messrs. Shivnarayan Surajmal Nemani to tax in respect of the commission for the period 1st April, 1944, to 31st December, 1944. We are sure that however grave the needs of the country may be, the Taxing Department will not seek to assess two parties in respect of the same income. The Department will have to make up its mind whether it wants to collect the tax from Messrs. Shivnarayan Surajmal Nemani or from the assesseees.

14. The assesseees to pay the costs.

15. Reference answered accordingly.