

(1924) 03 MAD CK 0049
In the Madras High Court

The Commissioner of Income Tax

APPELLANT

Vs

Binny and Co. Ltd.

RESPONDENT

Date of Decision : 27-03-1924

Acts Referred:

Citation : (1924) ILR (Mad) 837 : (1924) 47 MLJ 242

Hon'ble Judges : Victor Murray Coutts Trotter, C.J.; Ramesam, J

Bench : Full Bench

Judgement

Victor Murray Coutts Trotter, C.J.—This is a reference by the Commissioner of Income Tax which raises a very simple point in the sense

that it can be put within a narrow compass on a very few undisputed facts; in another sense it raised a subtle question of law, for it has given rise to

a great variety of judicial opinion in very high quarters.

2. Now the facts are these. A company called the Deccan Sugar and Abkari Co., Ltd. was incorporated in 1897 with a share capital of ten lakhs

in shares of Rs. 500 face value each. In May 1908, the capital was increased to 22 lakhs by adding 7,000 Preference Shares of the A class of Rs.

100 face value each and 5,000 Preference Shares of the B class also of Rs. 100 face value each. In 1908, in pursuance of a resolution passed in

June, the ordinary share capital was reduced to Rs. 1,66,672, thus making the total capital of the company something over 13 lakhs. Messrs.

Binny & Co., Ltd. held 200 ordinary shares of Rs. 125 each in this company. In 1921 the Deccan Company had on its books a surplus

accumulation of profits undistributed of practically 5 lakhs of rupees. In July 1921, by a special resolution, which was confirmed in the following

month, the Articles of the Company were amended, and the two important

amendments were these: The first was a preliminary one enabling the Company, by a special resolution, to sub-divide or consolidate its shares or any of them. The other was a new Article 133-A by which the Company, by a special resolution, may at any time take to itself the power to capitalise undivided profits or reserve fund : and that is what purported to take place in this case. Each holder of a share of Rs. 125 became the holder of three additional shares. The capital of the Company was increased by 1,328 shares of Rs. 375 each : and therefore the result was that Messrs. Binny & Co. for 200 shares of Rs. 125 each got 200 shares of Rs. 500 each, and in 1921 scrip carrying out that change of position was issued.

3. The question we have to decide is whether this issue of new shares to the share-holders representing their share to the accumulated surplus is

taxable as income. I propose to say very little about this matter, because, to my mind, it crystallises for our purposes into two questions. The first

is, are we concluded by the decision of the Privy Council in *The Swan Brewery Case* (1914) AC 231 The next is, are we at liberty, or is it

desirable if we are not covered by the Privy Council decision, to decide contrary to the majority of the House of Lords in *Blott's Case* (1921) AC

171

4. Now, it is best that I should deal with the first contention at the outset. It is suggested that *The Swan Brewery's Case* (1914) AC 231 directly

covers the present point, but with great respect to certain observations of Lord Sumner in *Blott's Case* (1921) AC 171. I am unable to say that it

does cover. If it does, of course, we as an Indian Court are not at liberty to say, as some of the members of the House of Lords did in *Blott's*

Case (1921) AC 171, that it was erroneously decided. If it does not decide the point finally for the House of Lords, it decides that finally and

conclusively for this Court. That was a decision on an Act known as the Dividend Duties Act of Western Australia, which, to put it shortly, taxed

dividends and contained a definition of "dividends, "which covered every profit, advantage or gain intended to be paid or credited to or distributed

among any members of any Company. It is quite obvious that a distribution of what was conveniently called Bonus shares is an advantage to the

share-holder, and therefore, one may conclude that, on the words of the Act,

their Lordships of the Privy Council had no option but to hold that this was a dividend within the meaning of the Act. Lord Sumner, in delivering the judgment of the Board said this : "In ordinary language the new shares would not be called a dividend, nor would the allotment of them be a distribution of a dividend" (it has to be observed that what is made taxable by the Act is a dividend and nothing more). "The question in issue, " his Lordship goes on, " here is whether or not the new, shares were a dividend under the Act above-mentioned. " Now, if that judgment stood alone unexplained by any subsequent utterance of his Lordship, I should infer that not merely was it a decision on the words of that statute but that it was care-fully confined to be a decision on the words of the Australian Statute with an intimation that, but for that statute the word could not be capable of bearing the meaning required to be put upon it before the Crown could succeed. But in Blott's Case (1921) AC 171 there is no doubt about it that Lord Sumner undoubtedly said that he had intended to lay down a wider principle, and that principle so far as I can see is this : Ever since the decision in Trevor and Witworth (1887) 12 AC 409 it has been the accepted law that a Company cannot buy its own shares. That is used as I follow the reasoning of Lord Sumner and Lord Dunedin to found this contention, that, as a Company cannot buy its own shares, that is to say, cannot pay its funds into its own coffers and issue scrip to itself, what must be supported to have taken place, as Lord Sumner says, notionally is that, although no such thing in fact happened, the company paid its profits over to the share-holder and that that share-holder repaid them and in return got scrip handed to him, which of course would give him a draft on the capital of the company. In my opinion, that reasoning is completely answered by the reasoning of Viscount Haldane and Viscount Finlay. I will just refer very briefly to one or two passages in Lord Finlay's judgment at page 192 of the report. He says this : "The general scope and effect of these transactions is beyond dispute. There was an increase in the capital of the company by the retention of the amounts available for dividends. Though the number of shares was increased by the issue of the new preference shares to the ordinary share-holders, this did not affect the proportions to which they were entitled in the undertaking and in any profits. All the share-holders received these new preference shares, so

that the proportion in which they were to share in any profits remained the same.... The use of the sums which had been available for dividend to

increase capital would enable the company to carry on a large and more profitable business, which might be expected to yield larger dividends.

These dividends, however, were to be in the future : so far as the present was concerned there was no dividend out of the accumulated profits;

these were devoted to increasing the capital of the company. "" Then again at page 194, "" The effect of this operation (that is, the one which he

described) was that the amount of the bonus was retained by the company as additional capital, and that the share-holders got the new preference

shares. No option was left to any particular share-holder. He was compelled by the action of the company to take the preference shares. He could

not have sued for the bonus in money as the resolution which gave the bonus *uno flatu* declared that it was to be satisfied by the distribution of

preference shares. Under these circumstances it seems to me impossible to treat the share-holders for the purpose of supertax as having received

the bonus and paid it back to the company to be retained as capital. They never received it at all. The case appears to stand exactly as *Rowlatt, J.*,

put it in *Inland Revenue Commissioners v. Blott and Inland Revenue Commissioners v. Greenwood* (1920) 1 KB 114; ""I do not think that there is

a payment of a dividend to a share-holder unless a part of the profits of the company is thereby liberated to him in the sense that the company parts

with it and he takes it. "" If I may humbly add a word in such a distinguished company I think it might be put in this way : "" That you cannot say that

there is a notional payment of a dividend to a share-holder when the position is that, if he sued for it his action must be dismissed. "" That is to say,

when the whole conception that he is entitled to the dividend is one that the law refuses to countenance. That being so, it is enough for me to say

that I think that this Court, having regard to the fact that the words of the Indian Statute are, for all practical purposes identical with those of the

English Statute, should respectfully follow the opinion of the majority of the highest Court in the Empire.

5. I must add this that, in doing so, the learned Lords were confirming the unanimous decision of a very strong Court of Appeal of three very

eminent Lords Justices. I may also add that of the majority of the House of Lords whose view prevailed, two at least were eminent and

distinguished Company Lawyers, and the dissentients were in the same unfortunate position as myself of being only common Lawyers. I should

also like to add this, that I think it is extremely improbable that this arrangement about the distribution of these profits and the manner in which the

transaction should be carried through was drafted without reference to the English cases. I do not know whether at the time the Resolution was

drafted the decision of the House of Lords was available, but, at any rate, the decision of the Court of Appeal in *Inland Revenue Commissioners v.*

Blott (1920) 1 KB 114, 133 and *Shone v. Greenwood* (1920) 2KB 657 was available. I have looked at that decision and it expresses the opinion

that that decision was determined by the decision in *Bouch v. Sproule* 12 AC 385, itself a House of Lords' decision, and that opinion of the Court

of Appeal must have been available to the learned gentleman who drafted these articles and amendments to articles. I also observe that both

Viscount Haldane and Viscount Cave agreed with the Court of Appeal in thinking that the matter before them in *Blott's Case* (1921) AC 171 is

concluded by the previous decision of the House of Lords. In these circumstances, although I have treated the matter as one of law, I think that it

would be an undesirable and inequitable result if we had to come to any other conclusion than that which I have arrived at.

6. Our answer to the reference is that the company *Messrs. Binny & Co.* is not liable to pay super-tax on the value of shares newly issued by the

Deccan Sugar and Abkari Co., Ltd. in the year 1921. The company will have its costs on the O.S. scale.

Ramesam, J.

7. I agree. There are three features in this case as in *Blott's Case* (1921) AC 171 which make it difficult for a Court to say that the additional

shares issued amount to income. The first is that there was no option to the shareholders, and it was not open to them to sue for the additional

dividend in the shape of cash or in the shape of other chattels or goods. The Resolution of the Company compelled them to take it only in the form

of additional shares and in no other. This feature was emphasised by all the Law Lords who formed the majority in *Blott's Case* (1921) AC 171.

The next feature which perhaps is a corollary from the first is this : The relative situation of each share-holder to the other share-holders in the

company remains unaltered. His proportion out of the total earnings that may be set apart for distribution as dividends among the share-holders

remains the same after this operation of the company. To explain it. further, if, for instance, in any year, the amount of profits that is set apart

available for distribution among the share-holders is one lakh, the proportion which a particular share-holder gets remains the same after the

increase in shares as before. If formerly a share-holder got 32 per cent, on shares of Rs. 125 each, now he will be getting Rs. 40 for each share of

Rs. 500, i.e., 8 per cent on shares of Rs. 500, the total income would be the same amount.

8. The third feature which again may be regarded as a corollary from the other two is that the effect is the same as if the company passed a

Resolution expanding its operations and for increasing its machinery. This has been pointed out by Viscount Finlay at page 196 in (1921) 2 A. C.

It is true that, as Lord Sumner points out, there was a payment in *Bouch v. Sproule* 12 AC 385, a dividend warrant was sent out in the form of a

negotiable instrument, which had it been presented payment must have been made. But this fact only served to distinguish *Bouch v. Sproule* 12 AC

385 from the case before the House of Lords in . If that distinction is emphasised, it follows that we ought to agree with the decision of the majority

in *Blott's Case* (1921) AC 171. It may be that the effect of the operations in question by the company is to increase the value of a share and, if a

particular share-holder sells his enhanced share, he may realise more in the market as pointed out by Viscount Cave. This amounts to only realising

his assets in the shape of capital and not in the shape of income.

9. I agree with the answer proposed by my Lord.