Privy Council Appeal No. 77 of 1946

The Bank of Chettinad, Ltd., of Colombo - - - *Appellant*

v.

The Commissioner of Income Tax, Colombo - - *Respondent*

FROM

THE SUPREME COURT OF THE ISLAND OF CEYLON

JUDGMENT OF THE LORDS OF THE JUDICIAL COMMITTEE OF THE PRIVY COUNCIL, DELIVERED THE 6TH APRIL, 1948

Present at the Hearing :

LORD SIMONDS
LORD MORTON OF HENRYTON
SIR MADHAVAN NAIR

[*Delivered by* LORD MORTON OF HENRYTON]

This appeal is concerned with the amount at which the appellant company (hereafter called " the company ") is liable to be assessed to income tax, under the Income Tax Ordinance of Ceylon, in respect of the income and profits of its Ceylon branch, conducted at an office in Colombo. The question for decision is whether, in computing the amount of the said income and profits, a deduction should be allowed in respect of a sum of Rs.53,226, debited to the Ceylon branch by way of interest on balances due to the head office during the year ending 31st March, 1940.

The answer to that question depends upon the construction of Rules made under the said Ordinance dealing especially with the taxation of the Ceylon branch of a non-resident bank, and upon the application of those Rules to the facts of the case. It has not been disputed that apart from these Rules, the deduction claimed is inadmissible, inasmuch as debits and credits as between a head office and the branches of a company are not expenses or receipts which come into account in computing the profits of the business of a branch.

The relevant portions of the Income Tax Ordinance No. 2 of 1932 and of the Rules made thereunder may be summarised as follows:—

In Section 2 of the Ordinance, which contains definitions, it is provided that—

> " ' banker ' means any company or body of persons carrying on the business of banking."

By Section 35 of the Ordinance it is provided that a non-resident person shall be assessable either directly or in the name of his agent, in respect of all his profits and income arising in or derived from Ceylon.

Section 90 empowers the Board of Income Tax to make Rules (inter alia) for the ascertainment or determination of any class of income, and in particular to prescribe the manner in which and the procedure by which the income, profits and gains shall be arrived at in the case of non-resident companies.

Rules have been made under Section 90 of the Ordinance with regard to the method of ascertainment and determination of the profits of Ceylon branches of non-resident bankers.

Rule 1 is as follows: —

In this rule, unless the context otherwise requires:

" bank " means any non-resident banker within the meaning of these expressions, as defined in Section 2 of Ordinance No. 2 of 1932.

" Ceylon branch " means the business carried on in Ceylon by any such bank.

" other branch " means the business carried on by a bank in any country outside Ceylon, including that carried on at its principal place of business.

The Rules provide for a deduction for interest where the Ceylon branch of a non-resident bank owes an average amount in an accounting period to other branches.

For reasons which will shortly appear, it is convenient to note that under section 330 of the Companies Ordinance No. 51 of 1938, a " banking company " is defined to mean " a company which carries on as its principal business the accepting of deposits of money on current account or otherwise, subject to withdrawal by cheque, draft or order, notwithstanding that it engages in addition in any one or more of the following forms of business ", which are then specified.

The company at the material time had its head office in Rangoon and a branch in Ceylon. It is common ground that the company was at that time a non-resident person, and that it carried on some business in Ceylon through its Ceylon branch. In the course of carrying on its business in Ceylon, the Ceylon branch credited a sum of Rs.53,226 to the head office in Rangoon by way of interest for the year ending on the 31st March, 1940. It was claimed by the company that this sum should be allowed as a deduction, under the Rules, in assessing the company in respect of the profits of the Ceylon branch for the year of assessment ending on the 31st March, 1941. The assessor having disallowed this claim, the company appealed to the respondent, who dismissed the appeal and confirmed the assessment, subject to an agreed deduction on other grounds.

In his determination, the respondent referred to the definition of a banking company contained in the Companies Ordinance, and took the view that the company did not come within that definition.

The company appealed to the Board of Review. That Board allowed the appeal and held that the company was entitled to the deduction claimed. The Board considered that the definition of " banking company " in the Companies Ordinance was not relevant to the construction of the Income Tax Ordinance. The respondent required the Board of Review to state a case on a question of law for the opinion of the Supreme Court, pursuant to Section 74 (1) of the Income Tax Ordinance, and a case was stated accordingly by the said Board.

It is convenient to quote the following passages from the case stated.

" At the hearing before the Commissioner it was not disputed that the Ceylon branch had been mainly carrying on the business of lending money on promissory notes or on the mortgage of immovable property in Ceylon and the management of estates and house properties owned by the Bank in Ceylon. The exhibit A (3) showed that the only Current and Deposit Accounts with the local branch were those of the Chettinad Corporation Limited, and seven other persons. These seven persons were stated to have closed their accounts during the year ending 31st March, 1940; thus the only current and deposit accounts as at that date were those of the Chettinad Corporation Limited, and these showed a debit balance as at

that date. That the branch was financed mainly from its Head Office in Rangoon appeared from the books. The Profit and Loss Account showed a sum of Rs.81,792 payable as interest by the local branch to the Head Office.

No cheque books have been issued by the Bank and no evidence was placed before the Commissioner that any moneys in deposit could have been withdrawn by cheque, draft or order."

No evidence was given by the company as to the amounts deposited by the above-mentioned seven persons, or as to the method by which these amounts were withdrawn. Other exhibits annexed to the case stated show that the Chettinad Corporation and the company were closely connected. Five individuals who held 99 per cent. of the issued capital of the Chettinad Corporation also held 95 per cent. of the issued capital of the company. The conclusions of the Board of Review are set out in paragraph 9 of the case stated, as follows:—

" (A) The Bank of Chettinad Limited, was at the material dates a " Non-resident banker " within the meaning of Rule I of the Rules made under Section 90 of the Ordinance, in that it carried on the business of a banker at its Head Office in Rangoon;

(B) The Ceylon Branch also carried on the business of a banker, on the facts before the Board;

(C) It is not necessary—in order to be entitled to the deduction claimed—that the business in Ceylon of the non-resident banker should be banking business.

If conclusion (A) is erroneous then the deduction would have to be disallowed whether or not conclusions (B) and/or (C) are correct. If conclusion (A) is correct then the deduction would have to be allowed in the event of either conclusion (B) or conclusion (C) being also held to be correct; but if (A) is correct and both (B) and (C) are incorrect then the deduction should be disallowed."

On the 17th January, 1946, the Supreme Court delivered judgment setting aside the Order of the Board of Review and declaring that the company was not entitled to the relief claimed. From that decision the company appeals.

It is convenient first to consider the Board's conclusion (C), and their Lordships feel no doubt that in arriving at this conclusion the Board of Review misconstrued the relevant statutory provisions. It is true that Rule I, in defining " Ceylon branch ", refers to " the business carried on in Ceylon by any such bank " and does not contain the words " of banking " after " business " but their Lordships think that these words must be implied. In their Lordships' view the rule-making authority must have contemplated that the business carried on by a bank at its branches would be banking business, and it was thought unnecessary to state this in terms. It is hardly to be supposed that if a non-resident bank chose to open and finance, for instance, a confectioner's business in Ceylon the deduction in question would be allowed in respect of such business. It would appear that no very strenuous effort was made in the Supreme Court to support conclusion (C), but as the point was not definitely abandoned their Lordships have allowed it to be raised before this Board.

As to conclusion (B), counsel for the company argued that this was a finding of fact in his favour by the tribunal entrusted with the duty of finding the facts. In their Lordships' view, however, the question whether the Ceylon branch carried on the business of banking at the relevant time is a question of mixed fact and law, involving the construction of the Ordinance and Rules. In a very clear and careful discussion of this question, the Board of Review referred to a number of authorities on the meaning of the words " banking " and " banker ". Their Lordships recognise that these words may bear different shades of meaning at different periods of history, and that their meaning may not be uniform

today in countries of different habits of life and different degrees of civilisation. For the purpose of this appeal, however, it is only necessary to ascertain what is meant by the words " business of banking " in an Ordinance applicable to Ceylon, which came into force in 1932. In their Lordships' view a valuable guide to the meaning of these words is afforded by Section 330 of the Companies Ordinance of 1938. In the Supreme Court Rose J., delivering a judgment with which the Acting Chief Justice agreed, held that Section 330, although it came into force six years later than the Ordinance of 1932, " merely crystallised what was already the legal conception of a bank in Ceylon ". Moreover, the definition in Section 330 in no way conflicts with the meaning attached to the word " banker " in England in 1932, and if Section 330 were to be entirely disregarded, it would be necessary to bear in mind the terms of Section 3 of the Civil Law Ordinance, 1853 (Cap. 66 of the Legislative Enactments of Ceylon) which provides as follows:

> " In all questions or issues which may hereafter arise or which may have to be decided in this Island with respect to the law of partnership, joint stock companies, corporations, banks, and banking, principal and agents, carriers by land, life and fire insurance, the law to be administered shall be the same as would be administered in England in the like case at the corresponding period if such question or issue had arisen or had to be decided in England, unless in any case other provision is or shall be made by any Ordinance now in force in this Island or hereafter to be enacted."

Their Lordships think that the proper test for determining whether the Ceylon branch carried on the business of banking at the material time is to consider whether that branch, at that time, could fairly be described as " a company which carries on as its principal business the accepting of deposits of money on current account or otherwise, subject to withdrawal by cheque, draft or order ". If this test is applied to the facts of the present case it becomes clear that there was no evidence upon which the Board of Review could properly find that the Ceylon branch answered that description. The passage quoted above from the case stated shows that the evidence was wholly inconsistent with any such finding. The accepting of deposits of money was clearly not the principal business of the Ceylon branch, and there was no evidence that any monies on deposit could have been withdrawn by cheque, draft or order. The Board of Review could not have arrived at conclusion (B) if its members had correctly interpreted the Ordinance and Rules, and the Supreme Court rightly rejected that conclusion.

As conclusions (B) and (C) are incorrect, the deduction claimed by the company must be disallowed and it is unnecessary to consider whether conclusion (A) is or is not correct. But their Lordships see no reason to differ from the observation of Rose, J. that the company might well experience difficulty in establishing that its head office in Rangoon was carrying on a banking business, within the meaning of the Ceylon Ordinance.

For these reasons their Lordships will humbly advise His Majesty that this appeal should be dismissed. The company must pay the respondent's costs of this appeal.

(59815) Wt. 8062—31 100 4/48 D.L. G. 338

In the Privy Council

THE BANK OF CHETTINAD LTD.,
OF COLOMBO

v.

THE COMMISSIONER OF INCOME TAX
COLOMBO

[DELIVERED BY LORD MORTON OF HENRYTON]

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