1958 *Present :* **Sansoni, J., and T. S. Fernando, J.**

THE COMMISSIONER OF INCOME TAX, Appellant, *and* SRI LANKA OMNIBUS CO., LTD., Respondent

S. C. 5—Case stated under Section 74 of the Income Tax Ordinance, BRA/254

Income tax—Omnibus company—Business carried on through agents—Computation of profits or income of the Company—Income Tax Ordinance, ss. 9 (1) (a), 9 (1) (cc) (i), 9 (1) (ccc) (i)—Agency—Test of relationship of principal and agent—Omnibus Service Licensing Ordinance, No. 47 of 1942.

A company which carried on, through agents appointed by it, the business of transport of passengers and goods under a licence issued in terms of the Omnibus Service Licensing Ordinance is entitled to claim deductions, under section 9 (1) (*a*) of the Income Tax Ordinance, for the depreciation by wear and tear of the buses owned by it, and, under section 9 (1) (cc) (i) or 9 (1) (ccc) (i), in respect of the cost of new buses purchased by it.

An agent, unlike an independent contractor, acts, on the whole, under the control of the principal. Where an omnibus company operates its business through " Branch Managers " appointed by it but retains in itself the general control of the running of the service, the relationship between the company and a " Branch Manager " is that of principal and agent.

CASE stated under section 74 of the Income Tax Ordinance.

M. Tiruchelvam, acting Solicitor-General, with *V. Tennekoon* and *H. L. de Silva*, Crown Counsel, for the Commissioner of Income Tax, appellant.

H. V. Perera, Q. C., with *H. W. Jayewardene*, Q. C., and *P. Ranasinghe*, for the assessee, respondent.

Cur. adv. vult.

May 15, 1958. T. S. FERNANDO, J.—

This case came to be stated in the following circumstances:

The assessee, the Sri Lanka Omnibus Company Ltd., a company incorporated under the Companies Ordinance, with the transport of passengers and goods as its principal object, commenced business on 16th January, 1943. The Omnibus Service Licensing Ordinance, No. 47 of 1942, had made legal provision for the introduction of a system of exclusive road service licences for omnibuses shortly before the establishment of the company, and the company was successful in obtaining licences in respect of a number of routes. The company took over 143 buses belonging to some 36 different owners who had prior to the enactment of the Ordinance been plying them in various sections of the routes allotted to the company. These owners were allotted shares in the company equivalent to the value of the buses, the goodwill and the value of the route licences held by them. Over one hundred of these buses belonged to seven individuals, while the balance belonged to others who owned one or two buses each. The seven individuals referred to above were elected directors of the company. The buses were run under a system called the Branch System, and seven branches were established with centres at seven different places, each in charge of a different director.

The terms and conditions under which these seven directors were to function were contained in letters addressed to each of them by the company, and document A.1 dated 28th December 1943 is a copy of a letter addressed to one of the directors, the letters to the other directors being similar to this in all relevant particulars. All seven directors were informed by these letters that they had been appointed the company's agents as from 16th January 1943 on the terms and conditions mentioned therein, and they all signified their acceptance of these appointments. Thereafter, by agreements dated 28th July 1947 entered into between the company and the seven agents appointed by the letters of 1943, the agents were designated Branch Managers, each for one of seven branches of the company which were to do the work formerly done by the respective agents. Document A.2 is one such agreement, the others being similar in all relevant particulars. One of the terms of these agreements was

that the Branch Manager should remit to the Sri Lanka Omnibus Company Ltd., the gross collections of fares after appropriating 90% of such gross collections for the payment of employees, for repairs, rents of garages, cost of petrol, oil, tyres and tubes, replacement of old buses, etc. Later, in April 1952, the Branch Managers handed over their functions under the agreements to companies formed by them and had these companies substituted in their respective places by agreements which they entered into with the Sri Lanka Omnibus Co., Ltd.. A.3 is a sample copy of these agreements. The seven directors who had first been the agents and later Branch Managers entered into agreements similar to A.3A guaranteeing the performance by the new companies of their respective functions under the agreements similar to A.3.

We are concerned in this case stated only with the assessments made upon the Sri Lanka Omnibus Co., Ltd., (which I shall hereafter refer to as the assessee-company) during the years of assessment (i) 1946-47 and (ii) 1948-49 to 1953-54. During these periods the Branch Managers furnished returns of income to the Income Tax Department on the basis that each of them was carrying on the business of transport of passengers at one or other of the seven centres referred to above, and were assessed on that basis. They did not claim, nor were they allowed, a deduction from their profits or income in respect of (1) depreciation of the buses or (2) the percentage fixed by law of the cost of the new buses purchased for the efficient running of the transport service. The assessee-company was assessed for income tax on the basis of its share of the 10% of the gross collections remitted by the Branch Managers in terms of the agreement A.2. A claim by the assessee-company to deduct, in computing its profits or income, (1) the depreciation of the buses in terms of section 9 (1) (*a*) of the Income Tax Ordinance and (2) a percentage of the cost of the new buses purchased in the relevant period in terms of section 9 (1) (*cc*) of the Ordinance was disallowed by the assessor. An appeal to the Commissioner having been unsuccessful, an appeal was preferred to the Board of Review which has held that the claim for both deductions should be allowed. The Commissioner, desiring to canvass the decision of the Board, has caused this case to be stated for determination by this Court.

The three questions which the Commissioner requested to be stated are set down as follows :—

(1) Whether the agreement dated the 29th day of July 1947—A.2—between the assessee-company and the person styled the Branch Manager therein can be deemed in law to have constituted the said person an agent of the assessee-company ?

(2) If the answer to (1) is in the negative, can the assessee-company be considered in law to have used their buses to carry on the business of transporting passengers or goods ?

(3) Whether, on the facts established in this case, the assessee-company is entitled in law to a deduction

(*a*) in such sum as the Commissioner considers reasonable under the provisions of section 9 (1) (*a*) for the depreciation by wear and tear of the buses owned by it ;

(*b*) under the provisions of sections 9 (1) (*cc*) (i) or 9 (1) (*ccc*) (i), in respect of the cost of buses purchased in its name during the years of assessment 1946-47 and 1948-49 to 1953-54 inclusive ?

At the commencement of the hearing before us, learned counsel who appeared for the assessee-company questioned whether any matter of law really arises upon this case stated. The objection, however, was not pursued, and the learned Solicitor-General who appeared for the Commissioner was permitted to argue the appeal. At the termination of the argument it appeared to us that the questions that do arise, viz. (*a*) whether the Branch Managers were agents of the assessee-company and (*b*) whether under the agreements the industrial undertaking was carried on by the assessee-company, were in reality questions of fact, and that in coming to its conclusion the Board of Review had not applied any wrong principles of law. Upon that view of the matter it does not appear to us that there was here any case to be stated under the provisions of section 74 of the Ordinance and, as there was evidence before the Board to support the decisions it reached, those decisions must stand.

At the same time as the questions stated were fully argued before us, I would like to examine the arguments. Before doing so, however, it is necessary to state that the deduction in terms of section 9 (1) (*a*) would be available to the assessee-company only if it could be established that the buses were used by it *in a trade or business carried on by it*, and that in terms of section 9(1) (*cc*) (i) or 9 (1) (*ccc*) (i) would be available only if the new buses *were purchased by it* and used in an industrial undertaking *carried on by it* in the relevant period. It may be mentioned that the expression "industrial undertaking" in section 9 (1) has been defined as meaning also an undertaking for transporting persons or goods.

The Solicitor-General contended that the arrang ment reached between the assessee-company and the Branch Managers constituted the latter not agents of the former but in reality independent contractors. He pointed to the fact that, as the Branch Managers have to pay to the assessee-company a sum of a rupee a day in respect of each bus given over to them, the buses which constituted the assessee-company's capital assets had been hired out by the assessee-company which thereby ceased to carry on the undertaking of transporting persons. As against this, it was urged on behalf of the assessee-company that this was accepted by the Commissioner as not being a hiring-out of the buses and no more than the making of a nominal payment to ensure that the title of the assessee-company to the buses would not be disputed by the Branch Managers. It appears not to have been disputed that a reasonable sum for the hire of a bus for a day would have to be estimated at about Rs. 100. In these circumstances the Board of Review appears to me to be justified in stating that this arrangement did not result in making the assessee-company a hirer of the buses.

The Solicitor-General next urged that there were other terms of the agreements which indicated that the real operators of the services were the Branch Managers, and that by entering into agreements like A. 2 and A. 3 the assessee-company had contracted away its rights to carry on the business which had in truth been assigned to the Branch Managers. Stress was laid on the fact that the buses were placed under the management of the respective Branch Managers who were to run the buses on the routes for which the assessee-company held the licences, maintain them in good repair, employ drivers or other employees at their expense, provide garage accommodation and indemnify the assessee-company for damage arising out of the negligence of the employees. On the other hand, counsel for the assessee-company pointed to other conditions in the agreement in support of his argument that, whatever be the terms between the parties, the true relationship between them was that of principal and agent. It was emphasized that the assessee-company could direct the Branch Managers to discontinue employees found to be unsatisfactory by the Board of Directors of the assessee-company, that the time and fare tables were prepared by the assessee-company and that the latter retained for itself the right to purchase new vehicles it considered necessary for the efficient running of the service although the purchase price fell to be paid by the Branch Managers out of the 90% of the collections they were permitted to retain. The Branch Managers were required to maintain proper waybills and returns, and the administration of the service was to be guided by the rules and regulations laid down by the Board of Directors of the assessee-company. The agreements stipulated that the Branch Managers shall faithfully and efficiently carry out the orders of the Board of Directors of the assessee-company. In these circumstances it is evident that on the whole the agreements preserved the control of the running of the service throughout in the assessee-company. It should be added that the assessee-company paid the licence fees for the buses and the premiums on the insurances obligatory under the Motor Car and the Workmen's Compensation Ordinances.

In considering the answers to the questions raised in this case it is not irrelevant to note that the running of a road service by any one of these Branch Managers without a licence in his name would have been illegal and that, although there has been no secrecy about the arrangement reached between the assessee-company and the Branch Managers, neither the Commissioner of Motor Traffic nor any other authority at any time took up the position that this arrangement was illegal. The amount of tax in dispute in this case is considerable, and it is significant that at no stage in these proceedings was it suggested that the arrangement evidenced by A.2 or A.3 was a blind. In the circumstances disclosed it would appear to me to have been difficult to maintain such a suggestion. I am of opinion that the Board of Review has rightly concluded that (1) the buses were used by the assessee-company in the business of the transport of persons carried on by it upon licence duly obtained therefor and (2) the new buses, although paid for in the first instance by the Branch Managers from the share of the collections retained by them, were purchased by the assessee-company as all the collections were in law money belonging to the assessee-company.

Certain authorities were cited before us at the argument, but it will suffice to mention only two of them. The learned Solicitor-General sought to find support for his contentions in the decision of the Court of Appeal in *The Union Cold Storage Co. Ltd. v. Jones* [1] where certain deductions claimed as representing (1) fire insurance premiums paid by a British Company in respect of certain premises and (2) wear and tear of machinery and plant were disallowed. The British company had transferred certain foreign cold storage business carried on by it to an American company for a term of years. The premises, machinery and plant of the foreign businesses remained the property of the British company, but they were placed under the sole control of and were used by the American company for the purpose of carrying on the businesses as it thought fit. They were not demised or leased to the American company and no rent was payable for their user, but the American company was to keep them in proper repair and working order, save as regards all ordinary wear and tear and damage by fire. In these circumstances it was held that the deductions claimed did not represent money wholly and exclusively laid out or expended for the purpose of the trade of the British company. This case is clearly distinguishable from the case before us where upon a construction of the agreements A.2 and A.3 it is evident that the Branch Managers were to carry on the business under the orders of the assessee-company.

The other case that might be examined is that of *London General Cab Co., Ltd. v. Commissioners of Inland Revenue* [2]. While there are certain superficial resemblances between the facts in that case and those in the case before us, it is clear upon a consideration of the judgment of Vaisey J. that the decision of the Court rested on the question whether the Cab Company was a " statutory undertaker " in whose favour there was an exemption from profits tax. A statutory undertaker was defined in the Finance Act of 1937, and the learned Judge came to the conclusion that the Cab Company did not come within that definition. There had been an admission before the General Commissioners that for certain purposes the relationship between the Cab Company and its drivers was that of bailor and bailee of the cabs. The decision of the Court turned on the admission, and upon this admission it was held that the relationship between the Cab Company and its drivers was not that of principal and agent or master and servant, and that the people who were really carrying on the business of transport of persons were not the Cab Company but the drivers who were the bailees under the agreement reached between them and the Company. The Solicitor-General argued that the relationship between the assessee-company and the Branch Managers was really that of bailor and bailee, but it seems to me to be impossible to say that the true construction of the agreements is not that reached by the Board of Review.

The appeal to this Court therefore fails and must be dismissed with costs.

SANSONI, J.—I agree.

Appeal dismissed.

[1] *(1924) 8 Tax Cases 725.*

[2] *(1959) 29 Tax Cases 407.*