Privy Council Appeal No. 108 *of* 1931.

The Commissioner of Income Tax, Bengal - - - *Appellant*

v.

Shaw, Wallace and Company - - - - - *Respondents*

FROM

THE HIGH COURT OF JUDICATURE AT FORT WILLIAM IN BENGAL.

JUDGMENT OF THE LORDS OF THE JUDICIAL COMMITTEE OF THE PRIVY COUNCIL, DELIVERED THE 14TH MARCH, 1932.

Present at the Hearing:

LORD BLANESBURGH.
LORD TOMLIN.
SIR GEORGE LOWNDES.

[*Delivered by* SIR GEORGE LOWNDES.]

This is an appeal from a judgment of the High Court at Calcutta delivered on a reference made to it under section 66 of the Indian Income Tax Act, XI of 1922. The reference arose out of an assessment to income tax upon the respondents for the year 1929–30, in respect of an item of Rs. 9,83,361, part of a larger sum of Rs. 15,25,000 received by them in 1928 as compensation for the termination of certain agencies.

The respondents carry on business in Calcutta as merchants and agents of various companies, and have branch offices in different parts of India. For a number of years prior to 1928 they acted as distributing agents in India of the Burma Oil Company and the Anglo-Persian Oil Company, but had no formal agreement with either company. In or about the year 1927 the two companies combined and decided to make other arrangements for the distribution of their products. The respondents' agency of the Burma Company was accordingly terminated on the

31st December, 1927, and that of the Anglo-Persian Company on the 30th June following. Some time in the early part of 1928 the Burma Company paid to the respondents a sum of Rs. 12,00,000 " as full compensation for cessation of the agency," and in August of the same year the Anglo-Persian Company paid them another sum of Rs. 3,25,000 as " compensation for the loss of your office as agents to the Company." The quotations are from letters by which the payments were recorded, and are accepted on both sides as correctly expressing the nature of the transactions.

The income tax officer, in computing the assessable income of the respondents for the relevant year, took these two receipts into account as profits or gains of their business in the year ending the 31st December, 1928, but allowed certain deductions therefrom in respect of compensation paid by the respondents to various employees, leaving a balance of Rs. 9,83,361 which he included in the total income of the respondents found assessable for the year 1929–30.

.The respondents objected to the assessment, and appealed to the Assistant Commissioner, who confirmed the assessment. Thereafter, on the requisition of the respondents, the Commissioner drew up a statement of the case, and referred the questions of law therein set out to the High Court with his own opinion thereon, which was against the contentions of the respondents.

The questions so formulated were as follows :—

(*a*) Was not the sum of Rs. 9,83,361 which had been included in the total income of the assessees for purposes of assessment for 1929–30, in the nature of a capital receipt and therefore not income, profits or gains within the meaning of the Income Tax Act ?

(*b*) If it could be said to be income, profits or gains within the meaning of the Act, was it liable to be assessed under either of the sections 10 and 12 of the Act, inasmuch as (1) it was not the profits, or gains of any business carried on by the assessees within the meaning of section 10 of the Act, nor (2) income, profits or gains from other sources within the meaning of section 12 of the Act ?

(*c*) In the alternative, was not the payment of Rs. 9,83,361 an *ex gratia* payment in the nature of a present from the oil companies in question and was it not therefore exempt under section (4) 3 (vii) of the Act ?

The reference was heard by the Chief Justice sitting with Ghose and Buckland JJ. The Judgment of the High Court was delivered by the Chief Justice, his colleagues concurring.

The learned Judges appear to have returned a formal answer only to question (*a*) which the Chief Justice stated to be " the real question in the case." He thought that if the respondents could not escape by reason of the contention raised by this question they must fail. The other questions, he thought, fell within a recent decision of the Court in the case of *In re Turner Morrison & Co.* reported in I.L.R. 56 Calc., 211 ; he had nothing to add to what was then said on these points.

Their Lordships agree that the real matter for decision falls under (*a*), but they think that this question is not happily worded,

as it seems to suggest that it was only if the sum there referred to was " in the nature of a capital receipt " that it would be exempt from assessment, whereas the more correct proposition would seem to be that it was only if it was in the nature of an income receipt that it would fall to be assessed to the tax. The question was, however, re-stated by the learned Chief Justice in more precise terms, viz., " whether these sums are income profits or gains within the meaning of the Act at all," and for the reasons stated in his judgment he came to the conclusion that they were not. Their Lordships think that his conclusion was right though they arrive at this result by a slightly different road.

In one part of his judgment the Chief Justice seems to hold that the " compensation for loss of these agencies is a receipt in respect of a capital asset in the nature of goodwill," but it has been objected with some force that there is nothing upon which this finding can be based. There was, so far as the facts disclose, no transfer of the goodwill of the respondents, and no agreement by them not to compete with the new selling agency of the companies.

In another part of the judgment the payment seems to be regarded as in the nature of compensation in lieu of notice. But here again their Lordships think that there are no facts to support such a conclusion, and they doubt if section 206 of the Indian Contract Act upon which reliance is placed has any application.

Again their Lordships would discard altogether the case law which has been so painfully evolved in the construction of the English Income Tax Statutes—both the cases upon which the High Court relied and the flood of other decisions which has been let loose in this Board. The Indian Act is not *in pari materia*; it is less elaborate in many ways, subject to fewer refinements, and in arrangement and language it differs greatly from the provisions with which the Courts in this country have had to deal. Under such conditions their Lordships think that little can be gained by attempting to reason from one to the other, at all events in the present case in which they think that the solution of the problem lies very near the surface of the Act, and depends mainly on general considerations.

The object of the Indian Act is to tax " income," a term which it does not define. It is expanded, no doubt, into " income profits and gains," but the expansion is more a matter of words than of substance. Income, their Lordships think, in this Act connotes a periodical monetary return " coming in " with some sort of regularity, or expected regularity, from definite sources. The source is not necessarily one which is expected to be continuously productive, but it must be one whose object is the production of a definite return, excluding anything in the nature of a mere windfall. Thus income has been likened pictorially to the fruit of a tree, or the crop of a field. It is essentially the

produce of something, which is often loosely spoken of as "capital." But capital, though possibly the source in the case of income from securities, is in most cases hardly more than an element in the process of production.

The sources from which the taxable income under the Act are to be derived are enumerated in Section 6, which runs as follows :—

> "Save as otherwise provided by this Act, the following heads of income, profits and gains, shall be chargeable to income-tax in the manner hereinafter appearing, namely :—
>
> (i) Salaries.
> (ii) Interest on securities.
> (iii) Property.
> (iv) Business.
> (v) Professional earnings.
> (vi) Other sources."

The claim of the taxing authorities is that the sum in question is chargeable under head (iv) business. By section 2 (4) business "includes any trade, commerce or manufacture, or any adventure or concern in the nature of trade commerce or manufacture." The words used are no doubt wide, but underlying each of them is the fundamental idea of the continuous exercise of an activity. Under section 10 the tax is to be payable by an assessee under the head business "in respect of the profits or gains of any business *carried on by him.*" Again, their Lordships think, the same central idea : the words italicised, are an essential constituent of that which is to produce the taxable income : it is to be the profit earned by a process of production. And this is borne out by the provision for allowances which follows. They include rent paid for the premises where the business is carried on ; the cost of current repairs in respect of such premises ; interest on money borrowed for carrying on the business, etc.

Some reliance has been placed in argument upon section 4 (3) (*v*) which appears to suggest that the word "income" in this Act may have a wider significance than would ordinarily be attributed to it. The subsection says that the Act "shall not apply to the following classes of *income,*" and in the category that follows, clause (v) runs :—

> "Any capital sum received in commutation of the whole or a portion of a pension, or in the nature of consolidated compensation for death or injuries, or in payment of any insurance policy, or as the accumulated balance at the credit of a subscriber to any such Provident Fund."

Their Lordships do not think that any of these sums, apart from their exemption, could be regarded in any scheme of taxation as income, and they think that the clause must be due to the over anxiety of the draftsman to make this clear beyond possibility of doubt. They cannot construe it as enlarging the word "income" so as to include receipts of any kind which are not specially exempted. They do not think that the clause is of any assistance to the appellant.

Following the line of reasoning above indicated, the sums which the appellant seeks to charge can, in their Lordships'

opinion, only be taxable if they are the produce, or the result, of carrying on the agencies of the oil companies in the year in which they were received by the respondents. But when once it is admitted that they were sums received, not for carrying on this business, but as some sort of *solatium* for its compulsory cessation, the answer seems fairly plain.

If the business had been sold—even if that somewhat indeterminate asset known as the " goodwill " had been assigned to the employing companies, as the High Court seems to have thought it had—it is conceded that the price paid would not have been taxable. But why ? Plainly because it could not be regarded as profit or gain from carrying on the business, and their Lordships think that the same reasoning must apply when the sum received is in the nature of a *solatium* for cessation.

It is contended for the appellant that the " business " of the respondents did in fact go on throughout the year, and this is no doubt true in a sense. They had other independent commercial interests which they continued to pursue, and the profits of which have been taxed in the ordinary course without objection on their part. But it is clear that the sum in question in this appeal had no connection with the continuance of the respondents' other business. The profits earned by them in 1928 were the fruit of a different tree, the crop of a different field.

For the reasons given their Lordships are of opinion that question (*a*) was rightly answered by the High Court in favour of the assessee. No objection has been taken to the form of the answer or to its sufficiency, and it would seem unnecessary therefore to deal with the other two questions. Their Lordships will only add that the reasoning of this judgment would apply equally if the appellant based his claim on head (vi) " other sources " and the corresponding provisions of section 12.

With regard to the claim to exemption under section 4 (3) (vii), their Lordships think that the decision in the case of *In re Turner Morrison & Co.* to which reference has been made above, may need re-consideration in the light of this judgment. In their Lordships' view the expression " receipts arising from business " in that clause must mean receipts arising from the carrying on of business.

Their Lordships will humbly advise His Majesty that this appeal should be dismissed with costs.

In the Privy Council.

THE COMMISSIONER OF INCOME TAX, BENGAL,

v.

SHAW, WALLACE AND COMPANY.

DELIVERED BY SIR GEORGE LOWNDES.

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