Commissioner Of Income-Tax, Punjab, ... vs Prabhu Dayal (Decd., By Legal ... on 6 October, 1971

Equivalent citations: AIR1972SC386, [1971]82ITR804(SC), (1972)4SCC517, [1972]1SCR991, AIR 1972 SUPREME COURT 386, 1972 4 SCC 517, 1972 TAX. L. R. 163, 1972 (1) SCR 991, 1972 (1) ITJ 573, 1974 SCC (TAX) 351, 82 ITR 804, 1972 2 SCJ 102

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Bench: A.N. Grover, H.R. Khanna, K.S. Hegde

JUDGMENT

K.S. Hegde, J.

1. This is an appeal by certificate from the decision of the High Court of Punjab and Haryana in a Reference under Section 66(1) of the Indian Income-tax Act, 1922 (to be hereinafter referred to as the Act). The question referred to the High Court for its opinion was:

> Whether on the facts and in the circumstances of the case, the receipt of Rs. 70,000/-by the assessee on 11-6-1954 was revenue or capital in nature.

2. The High Court held that the said receipt was capital receipt. Aggrieved by that decision the Commissioner of Income-tax came up in appeal to this Court.

3. We shall now refer to the material facts found by the Income-tax Appellate Tribunal as can be gathered from the case stated. The assessee was assessed as an individual. The relevant assessment year is 1955-56, the accounting period for the same ended on Asad sudi 1, S.Y. 2011.

4. The assessee was instrumental in discovering the existence of Kankar deposits in Jind State. He also brought about an agreement between one Shanti Parsad Jain and the erstwhile State of Jind, now a part of Punjab State for the acquisition of sole and exclusive monopoly rights of manufacturing cement in the said Jind State. That agreement was entered into on April 2, 1938. The same was to remain operative for a period of 25 years, which term was liable to be extended to 100 years at the option of the said Shanti Parsad Jain or his nominee. Shanti Parsad Jain transferred his rights under that agreement to a public limited company by name M/s. Dalmia Dadri Cement Ltd. on May 4, 1938. The assessee was one of the promoters of the said company.

5. For the services rendered by the assessee, the Dalmia Dadri Cement Co. by an agreement dated May 27, 1938 agreed, to pay him a commission of 1% on the yearly net profits earned by the company from the said cement factory. That agreement was to subsist so long as the original agreement dated April 2, 1938 subsisted.

6. The agreement dated May 27, 1938 between the assessee and the Dalmia Dadri Cement Co. was acted upon till 1950 and thereafter the company did not pay the commission agreed to be paid. Consequently the assessee filed a suit against the company claiming the commission due to him. The said suit ended in a compromise and the compromise was made a decree of court. Under that decree the assessee was to be paid Rs. 15,000/ as commission for the years 1951 and 1952 and Rs. 15,000/-as commission for the year 1953. Further he was to be paid Rs. 70,000/-by way of compensation for the termination of the agreement between him and the company as from January 1, 1954. That compensation was received by the assessee on June 11, 1954.

7. The assessee's claim that the sum of Rs. 70,000/-was capital receipt and hence not taxable in his hands was rejected by the Income-tax Officer. That officer held that the said sum of Rs. 70,000/-was a remuneration paid once and for all for the services rendered by the assessee and as such taxable in his hands. This decision was affirmed by the Appellate Assistant Commissioner, who held that the amount of Rs. 70,000/-was a lump sum compensation received for the services rendered; hence the same was a receipt in the ordinary course of assessee's business and consequently it was taxable as a revenue receipt.

8. Aggrieved by that order the assessee took up the matter in appeal to the Tribunal. The Tribunal held that the company by paying the said compensation of Rs. 70,000/-terminated the contract which enabled the assessee to receive from the said company a commission of one per cent of the net profits and as such the said receipt by the assessee was capital and not revenue.

9. Thereafter at the instance of the Commissioner the question set out earlier was referred to the High Court for its opinion which, as mentioned earlier, was answered in favour of the assessee.

10. It was not the case of the Revenue that the assessee was engaged in the business of discovering Kankar or any other mineral. He appears to have found Kankar by mere chance. It is also not the case of the Revenue that the assessee was engaged in the business of bringing about agreements between parties. In fact, it is not the case of the Revenue that the assessee was engaged in any business. There is no evidence to show that he was a business man. His discovery of Kankar as well as his part in bringing about the agreement mentioned earlier were stray acts, possibly occasioned by fortuitous circumstances.

11. Business as understood in the income-tax law connotes some real, substantial and systematic or organised course of activity or conduct with a set purpose-see the decision of this Court in Narain Swadeshi Weaving Mills v. Commissioner of Excess Profits Tax 26 I.T.R. 765. By this statement we do not mean to say that under no circumstance a single transaction cannot amount to a business transaction. But this is not one such. Herein we are dealing with the stray activity of a non-business man. Hence it is difficult to agree with the Revenue in its contention that the agreement entered into

by the assessee with the Dalmia Dadri Cement company should be considered as a business activity.

12. In the determination of the question whether a particular receipt is capital or an income, it is not possible to lay down any single test as infallible or any single criterion as decisive. The question must ultimately depend on the facts of the particular case and the authorities bearing on the question are valuable only as indicating the matters that have to be taken into account in reaching a decision. That, however, is not to say that the question is one of fact, for these questions between capital and income, trading profit or no trading profit, are questions which, though they may depend to a very great extent on the particular facts of each case, do involve conclusions of law to be drawn from those facts-see Commissioner of Income-tax Nagpur v. Rai Bahadur Jairam Valij and Ors. 35 I.T.R. 148.

13. The controversy whether a particular receipt is capital or revenue has engaged the attention of this Court as well as of the High Courts in numerous cases. It is, by no means an easy question to decide. It is neither feasible nor profitable to refer to those cases because in the ultimate analysis the decision in those cases rests on the facts of each case. But the case nearest to the case before us is that decided by the House of Lords in Van Den Berghs Ltd. v. Clark 19 Tax Cases 390 : (1935) 3, I.T.R. Supp. 17. The facts of that case were as follows:

> The assessee therein received a sum of £ 450,000 in full settlement of all claims and counter-claims which existed between the assessee and a Dutch company. Both the companies had been engaged in the business of manufacturing and dealing in margarine and similar products. They had entered into pooling arrangements at as early a date as in 1908 under which they bound themselves to work in friendly alliance and to share their profits of their respective business in margarine in specified proportions. This basic agreement of 1908 was being added to and varied from time to time particularly in 1913 and 1920 and, under this, the agreement was to subsist until 1940. In 1922 the assessee made a claim against the Dutch company for about £ 450,000 as the amount due to it by the Dutch company under the agreements recited just previously. This was however repudiated and the Dutch company claimed that far from owing any moneys to the assessee, moneys were owing to them. One of the methods suggested for putting an end to the dispute was by a termination of the agreement between the two companies but this was resisted by the assessee company. A settlement was, however, reached in 1927.whereby in consideration of the payment by the Dutch company of £.450,000 to the assessee as damages, the agreements were determined as at 31st December, 1927 and each party released the other from all claims thereunder. The question was whether this sum of £ 450,000 was a revenue receipt on which the income-tax could be levied against the assessee. The matter came up before Finlay J. He held against the Crown. According to him the sum received was not a revenue receipt. This decision was reversed by the Court of Appeal but was restored on a further appeal by the House of Lords. Finlay J. in the course of his judgment formulated the question to be considered by him in these terms:

> I agree with Mr. Latter that there are three questions here. The first is: What was this payment for ? The second is: If a payment for future rights, is it assessable ? The third question is: Ought it to go into the year 1927.

14. The learned judge's answer to the first question was that it was a payment for future rights. He held that it was really a payment for cancelling such rights as subsisted in the assessee between 1928 and 1940. Having answered the first question in that manner the learned judge held on the second question that it was not assessable. In arriving at that conclusion he reasoned thus:

> Not without hesitation, I have come to the conclusion that it is not liable to assessment. I think that the agreement being an agreement whereby this company had a share in the profits of another company, was a capital asset. I think that the case is to be distinguished from the case where there is a cancellation of a contract made in the ordinary course of the company's business.... But it seems to me that where one gets, as one does here, not a contract made in the course of the company's business-for it is not the business of this company to make pooling agreements or to make agreements whereby they acquired shares in the business of another company-it seems to me that where one gets a payment made in respect of the cancellation of that agreement, that, truly is a sum received by way of capital and not an income receipt at all.

15. Lord Macmillan who delivered the leading judgment of House Lords put the case thus:

> Now what were the appellants giving up? They gave up their whole rights under the agreements for thirteen years ahead. These agreements are called in the stated cases 'pooling agreements' but that is a very inadequate description of them, for they did much more than merely embody a system of pooling and sharing profits. If the appellants were merely receiving in one sum down aggregate of profits which they would otherwise have received over a series of years, the lump sum might be regarded as of the same nature as the ingredients of which it was composed. But even if payment is measured by annual receipts, it is not necessarily in itself an item of income.... The three agreements which the appellants consented to cancel were not ordinary commercial contracts made in the course of carrying on their trade; they were not contracts for the disposal of their products or for the engagements of agents or other employees necessary for the conduct of their business: nor were they merely agreements as to how their trading profits when earned should be distributed as between the contracting parties. On the contrary, the cancelled agreements related to the whole structure of the appellant's profit making apparatus. They regulated the appellant's activities, defined what they might and what they might not do and affected the whole conduct of their business. I have difficulty in seeing how money laid out to secure, or money received for the cancellation of, so fundamental an organisation of a trader's activities can be regarded as an income disbursement or an income receipt'.... In my opinion that asset, the congeries of rights which the appellants enjoyed under the agreements and which for a price they surrendered was

a capital asset.

16. It is now well settled that a distinction has to be drawn between a payment made for past services or discharge of past liabilities and that made for compensation for termination of an income producing asset. The former does not lose its revenue nature but the latter being a payment for destruction of a capital asset, must be considered as capital receipt.

17. The distinction between a capital receipt and a revenue receipt came up for consideration before this Court in Senairam Doongarmal v. Commissioner of Income-tax, Assam 42 T.T.R. 392. The assessee therein owned tea estate consisting of tea gardens, factories and other buildings, carried 0:1 a business of growing and manufacturing tea. The factory and other buildings on the estate were requisitioned for defence purposes by the military authorities. The assessee continued to be in possession of the tea gardens and tended them to preserve the plants but the manufacture of tea was completely stopped. The assessee was paid compensation for the year 1944-45 under the Defence of India Rules calculated on the basis of the out-turn of tea that would have been manufactured by the assessee during that period. The question was whether the amounts of compensation were revenue receipts taxable in the hands of the assessee. This Court held that the first consideration before holding a receipt to be profits or gains of business within Section 10 of the Income-tax Act was to see if there was a business at all of which it could be said to be income. The primary condition of the application of Section 10 was that tax was payable by an assessee under the head "Profits and gains of a business" in respect of a business carried on by him. Where an assessee did not carry on business at all the section could not be made applicable and any compensation for requisition of assets that he received could not bear the character of profits of a business. The Court further held that the amounts of compensation received by the assessee were not revenue receipts and did not comprise any element of income. It is true that in that case the Court did not consider whether the income in question could have been considered as income from other sources but the ratio of that decision is that the compensation paid being in respect of sterilisation of an income producing asset, the same should be considered as a capital receipt.

18. The only other decision we need make reference is the decision of this Court in Kettlewell Bullen and Co. Ltd. v. Commissioner of Income-tax, Calcutta, 53, I.T.R. 261. Therein this Court observed that it cannot be said as general rule that what is determinative of the nature of a receipt on the cancellation of a contract of agency or office is extinction or compulsory cessation of the agency or office. Where payment is made to compensate a person for cancellation of a contract which does not affect the trading structure of his business or deprive him of what in substance is his source of income, termination of the contract being a normal incident of the business and such cancellation leaves him free to carry on his trade though freed from the contract terminated, the receipt is revenue; where by the cancellation of an agency the trading structure of the assessee is impaired, or such cancellation results in loss of what may be regarded as the source of the assessee's income, the payment made to compensate for cancellation of the agency agreement is normally a capital receipt. These decisions lay down the tests to be applied in distinguishing a capital receipt from a revenue receipt. With the guidance thus afforded, let us now take a second look at the facts found for answering the question referred. The assessee, possibly, by some fortuitous circumstance discovered Kankar in some place in Jind State. This circumstance gave him an oppurtunity to bring about an

agreement between the State of Jind and Shanti Prasad Jain and when Shanti Parsad Jain transferred his right to a new company, in the formation of which the assessee had a hand, he was promised certain yearly commission on the net profits earned by the company. None of these activities of the assessee can be considered as a business activity but yet he did acquire an income yielding asset as a result of his activities. But the compromise decree destroyed that asset and in its place he was given Rs. 70,000 a compensation. This payment was neither in respect of the services rendered by him in the past nor towards the accumulated commission due to him. It was paid as compensation to him because he gave up his right to get commission in future to which he was entitled under the agreement. It was a price paid for surrendering a valuable right which in our opinion was a capital asset. Therefore that receipt must be considered as a capital receipt.

19. For the reasons mentioned above this appeal fails and the same is dismissed with costs.