New Savan Sugar & Gur Refining Co. Ltd vs Commissioner Of Income-Tax, Calcutta on 19 February, 1969

Equivalent citations: 1969 AIR 1062, 1969 SCR (3) 761, AIR 1969 SUPREME COURT 1062

Author: V. Ramaswami

Bench: V. Ramaswami, J.C. Shah, A.N. Grover

PETITIONER:
NEW SAVAN SUGAR & GUR REFINING CO. LTD.

Vs.

RESPONDENT:
COMMISSIONER OF INCOME-TAX, CALCUTTA

DATE OF JUDGMENT:
19/02/1969

BENCH:
RAMASWAMI, V.
BENCH:
RAMASWAMI, V.
SHAH, J.C.
GROVER, A.N.

CITATION:
1969 AIR 1062 1969 SCR (3) 761
1969 SCC (1) 621
CITATOR INFO :
D 1988 SC 460 (12)

ACT:
Income-tax Act (11 of 1922), ss. 10(2)(vi-a) and (vi-b) and 12(3) and (4)-Scope of s. 10-If cls. (vi-a) and (vi-b) of s. 10(2) could be read by implication into s. 12.

HEADNOTE:
The assessee-company, carrying on the business of crushing sugar cane and gur refining, apprehending loss, entered into a lease with another company. Under cl. (7) of the indentures the consideration of the lease. was royalty payable on the manufacture of sugar and molasses and was, subject to a minimum payment of Rs. 65,000 per annum. The

lease was. for a term of 5 years commencing from 1st June 1945 with an option to continue for a further term of 5 years and thereafter with two further options of 5 years on the same terms and conditions subject to payment of higher rates of royalty. Clauses 2 to 5 provided that the existing machinery which was owned by the lessor could not be removed and that the lessee would be entitled to set up additional machinery without interference from the lessor and that on the termination of the lease the lessee would be entitled to remove the same without causing any damage to the property demised. The effect of cls. 11 to 14 was that the lessor would have no concern with the production of the factory which was the principal part of the business previously carried on by the lessor. In assessment proceedings for the assessment year 1955-56, the assessee contended that the lease was a lease of a commercial asset and therefore the income arising from it should be assessed under s. 10 of the Income-tax Act, 1922, and hence, the assessee should be allowed depreciation and development rebate in accordance with cls. (vi-a) and (vi-b) of s. 10(2). The department and the High Court rejected the assessee's contention and held that the income was liable to be assessed under s. 12 as 'income from other sources' and that no additional depreciation and development rebate could be allowed.

In appeal to this Court it was contended that : (1) the income of the assessee was liable to be assessed under s. 10 of the Income-tax Act and, not under s. 12; and (2) Since the benefit under cl. (vi) of s. 10(2) is allowed to the assessee under s. 12(3), the assessee should be held to be entitled to additional depreciation and development rebate under cls. (vi-a) and (vi-b) even if the assessment was under s. 12, on the ground that those two clauses are ancillary to cl. (vi) and should be taken to have been included in s. 12(3) along with cl. (vi).

HELD : (1) The income of the assessee could not be characterised' as income from the activity of the assessee carrying on any business and' was therefore, liable to be assessed under s. 12 and not under s. 10 of the, income-tax Act. [769 F-G]

The primary condition for the application of s. 10 is that the tax is payable by an assessee under the head 'profits and gains of business' in respect of business carried on by him. When an assessee does not carry on business at all, s. 10 cannot be applicable and the income that he receives cannot bear the character of profits of business. [769 D-E] 762

In the present case, a scrutiny of all the clauses of the indenture of lease, shows that the intention of the assessee was to go out of the business altogether, so far as the factory and machinery were concerned with effect from 1st June 1945, to part with the entire machinery of the factory and the premises with the purpose of earning rental income, and to use the income arising from the royalty in its

capacity as owner of the factory. It was not the intention of the assessee to treat the factory and machinery as a commercial concern or asset during the subsistence of the lease. The provision for payment of minimum royalty indicates that the assessee had no direct interest in the production of the factory. The royalty was not paid for the production in the factory. There was no direct nexus between the income of the assessee and the production of the factory. The production was only a measure of the royalty to be paid and had nothing to do with the character of the payment as a receipt from business or from other sources. [769 C-D, E-F]

Commissioner of Excess Profit Tax, Bombay City v. Shri Lakshmi Silk Mills Ltd. 20 I.T.R. 451 (S.C.) and Narain Swadeshi Weaving Mills v. Commissioner of Excess Profits Tax, 26 I.T.R. 765 (S.C.), distinguished.

(2)Clause (vi-a), which was inserted in the Act in 1949, gives additional depreciation allowance over and above the initial allowance which was previously available under cl. (vi) in respect of buildings newly erected and new machinery and plant but not furniture installed after 31st March 1948. The additional allowance is confined to not more than 5 successive assessments falling within the period from 1st April 1949 and 31st March 1959. It is deductible in determining the written down value, unlike the initial allowance granted under cl. (vi). Clause (vi-b) was inserted by the Finance Act, 1955. It grants development rebate in respect of machinery and plant provided that the machinery or plant is new and has been installed after 31st March 1954, and provided further that it is used wholly for the purpose of the assessee's business and the particulars prescribed for the purpose of cl. (vi) have been furnished. Clauses (Vi-a) and (vi-b) thus introduce a new scheme and cannot be treated as an integral part of cl. (vi) by implication. Further, it is not permissible for the Court to read the-clauses by implication into s. 12(3) and (4), because, the clauses were not specifically engrafted by Parliament into s. 12 while amending s. 10(2). [771 E-H; 772 A-B] Kumar Kamalaranjan Roy v. Secretary of State, L.R. 66 I.A. 110, referred to.

JUDGMENT:

CIVIL APPELLATE JURISDICTION: Civil Appeal No. 1593 of 1968. Appeal from the judgment and order dated, September 20, 1963 of the Calcutta High Court in Income-tax Reference' No. 23 of 1960.

Sachin Chaudhari, T. A. Ramachandran and D. N. Gupta, for the appellant.

D.Narsaraju, R. N. Sachthey and B. D. Sharma, for the respondent.

The Judgment of the Court was delivered by Ramaswami, J This appeal is brought by certificate from the judgment of the Calcutta High Court dated 20th September, 1963 in Income Tax Reference No. 23 of 1960.

The appellant (hereinafter referred to as the assessee was carrying on the business of crushing sugar-cane and gur refining. M/s. Andrew Yule & Co. were acting as the managing agents of the assessee. In a letter dated 5th February, 1946 addressed to the share-holders of the assessee the managing agents referred, to the alarming increase of Government interference in the affairs of the sugar industry in Bihar and the increase of wages of the workers, as well as the levy of a cess of Government and deterioration in the cane crops. In view of this state of affairs, the managing agents apprehended a loss and suggested that the company's affairs should be put on a "less discouraging basis" by accepting the offer of a lease of the company as a running concern from the Standard Refinery & Distillery Ltd. At an extra-ordinary general meeting of the share-holders of the assessee company held on 5th March, 1946 it was decided to authorise the directors to enter into a lease with the said Standard Refinery & Distillery Ltd. By an indenture of 15th March, 1948 the lease was executed to come into effect retrospectively from 1st June, 1945. The term of the lease was originally for 5 years commencing from 1st June 1945 with an option to the lessee to continue for further five years and thereafter two further options to the lessee, each for five years, on the same terms and conditions, but subject to the payment of higher rates of royalties and also subject to the option on the part of the assessee company to terminate the lease by a resolution of the shareholders of the company to be held before 30th November in any year after the first two years. This option of termination of the lease was not exercised by the assessee company. The consideration of the lease as described in clause 7 of the indenture was royalty payable on the manufacture of sugar and molasses. The royalty on sugar was to be at the rate of Rs. 75 per hundred maunds of sugar manufactured for the first and second term of five years, at the rate of Rs. 82.50 per hundred maunds of sugar manufactured for the third five year period and at Rs. 90 for the fourth five year period. The royalty on molasses was to be calculated at 3 pies per maund on all molasses sold during each year of the original period or the renewed period of the lease. The computation of the royalty was subject to a minimum payment of Rs. 65,000 per annum. For the assessment year 1955-56 the relevant accounting year of the assessee ended on 31st May, 1954. In the assessment proceedings for 1955-56 the assessee's main contention was that the lease granted under the indenture of 15th March, 1948 was a lease of a commercial asset and therefore the income arising from the lease should be assessed under S. 10 of the Income Tax Act and the assessee should be allowed depreciation and development rebate in accordance with clause (vi-a) and clause (vi-b) of sub-section (2) of section 10 of the Income Tax Act. The Income Tax Officer assessed the income under S. 12 of the Act as being income under the head "other sources" and held that no additional depreciation or development rebate could be allowed as claimed by the assessee. According to the assessee, the, income derived from the lease of the sugar factory was income from business because the factory was leased as a going concern and the rent of the building, machinery, plant and spare parts was fixed at a certain rate per maund of sugar produced, and at a certain rate per maund of molasses sold. On appeal, the Appellate Assistant Commissioner found that it was a simple lease of the building and machinery in a sugar factory, and as such the method of payment based on production could not affect the character and nature of the income derived under the said lease. In further appeal the Appellate Tribunal came to the conclusion that on the facts stated the case fell

under section 12 and not under section 10 and that since sub-section (3) of section 12 did not include clauses (vi-a) and (vi-b) of section 10(2) the claim of additional depreciation and development rebate could not be allowed. At the instance of the assessee the Appellate Tribunal stated a case to the High Court on the following questions of law under section 66(1) of the Income Tax Act, 1922 (hereinafter referred to as the Act) :

> "(1) Whether on the facts and in the circumstances of the case, the income of the assessee company was liable to be assessed under section 12 of the Indian Income Tax Act and not under section 10 of the said Act ? (2)Whether on the facts and in the circumstances of the case, additional depreciation and development rebate can be allowed as a deduction ?"

The High Court answered both the, questions against the assessee holding that the income was liable to be assessed under section 12 and that no additional depreciation and development rebate could be allowed.

Section 10 of the Act stood as follows at the material time "10. (1) The tax shall be payable by an assessee under the head 'profit sand gains of business, profession or vocation' in respect of the profit or gain of any business, profession or vocation carried on by him. (2)Such profits or gains shall be computed after making the following allowances, namely

(vi)in respect of depreciation of such buildings, machinery, plant or furniture being the property of the assessee, a sum equivalent, where the assets are ships other than ships ordinarily plying on inland waters, to such percentage on the original cost thereof to the assessee as may in any case or class of cases be prescribed and in any other case, to such percentage on the written down value thereof as may in any case or class of cases be prescribed :

> and where the buildings have been newly erected, of the machinery or plant being new, not being machinery or plant entitled to the development rebate under, clause (vi-b), has been installed, after the 31st day of March, 1945, a further sum (which shall however not be deductible in determining the written down value for the purposes of this clause) in respect of the year of erection or installation equivalent--
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> (a) in the case of buildings the erection of which is begun and completed between the 1st day of April 1946 and the 31st day of March 1956 (both days inclusive), to fifteen per cent of the cost thereof to the assessee;
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> (b) in the case of other buildings, to ten per cent of the cost thereof to the. assessee;
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> (c) in the case of machinery or plant, to twenty per cent of the cost thereof to the assessee;

Provided that-

(c)the aggregate of all allowances in respect of depreciation made under this clause and clause (vi-a) or under any Act repealed hereby, or under the Indian Income Tax Act, 1886 (II of 1886), shall, in no case, exceed the original cost to the assessee of the buildings, machinery, plant or furniture, as the case may be;

(vi-a) in respect of depreciation of buildings newly erected, or of machinery or plant being new which has been installed, after the 31st day of March, 1948, a further sum (which shall be deductible in determining the written down value) equal to the amount admissible under clause (vi) (exclusive of the extra allowance for double or multiple shift working of the machinery or plant and the initial depreciation allowance admissible under that clause for the first year of erection of the building or the installation of the machinery or Plant) in not more than five successive assessments for the financial years next following the previous year Sup/69-14 in which such buildings are erected and such machinery and plant installed and falling within the period commencing on the 1st day of April 1949 and ending on the 31st day of March, 1959;

(vi-b) in respect of machinery or plant being new, which has been installed after the 31st day of March, 1954, and which is wholly used for the purposes of the business carried on by the assessee, a sum by way of development rebate in respect of the year of installation equivalent to twenty-five per cent of the actual cost of such machinery or plant to the assessee;

Provided that no allowance under this clause shall be made unless the particulars prescribed for the purpose of clause (vi) have been furnished by the assessee in respect of such machinery or plant;

Section 12 was to the following effect

12. (1). The tax shall be payable by an assessee under the head 'Income from other sources' in respect of income, profits and gains of every kind which may be included in his total income (if not included under any of the preceding heads).

(2)Such income, profits and gains shall be computed after making allowance for any expenditure (not being in the nature of capital expenditure) incurred solely for the purpose of making or earning such income, profits or gains.

(3)Where an assessee lets on hire machinery, plant or furniture belonging to him, he shall be entitled to allowances in accordance with the provisions of clauses (iv), (v), (vi) and

(vii) of sub-section (2) of section 10.

(4)Where an assessee lets on hire machinery, plant or furniture belonging to him and also buildings, and the letting of the buildings is inseparable from the letting of the said machinery, plant or furniture, he shall be entitled to allowances in accordance with the provisions of clauses (iv), (v), (vi) and

(vii) of subsection (2) of section 10 in respect of such buildings".

The main contention of the assessee was that the lease as contemplated in the indenture dated 15th March, 1948 was a lease of a commercial asset, and, therefore, the income arising from the lease should be assessed under section 10(1) of the Act and not under section 12(1). In order to examine the validity of this argument it is necessary to set out the relevant clauses of the indenture of lease. Clause (1) of the lease provided that the lease was for a term of five years commencing from 1st June 1945 with an option to continue for a further term of five years and thereafter two further options of five years in each case on the same terms and conditions subject to higher payment of rates of royalties.

Clause 2:

> The lessee shall be entitled to run the said sugar factory and all other machinery annexed to the same and use all the tools and implements, buildings and premises, offices, and erections and utensils and all other things which are now in or upon the said premises and which may be added from time to time thereto provided always that the lessees shall not at any time remove the plant and/or machinery etc. hereby demised or any part thereof from the said premises elsewhere for the purpose of or in connection with the lessees' other interests.
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> Clause 3 :
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> The lessees shall at the time of taking over possession of the factory from the lessors be entitled free of payment to the goods already manufactured during the current crushing season, i.e. 1945-46 or in the process of manufacture and/or to be hereafter manufactured by the lessees and the lessees shall have absolute discretion to sell and deal with the same in such manner as they think fit and proper.
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> Clause 5:
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> The lessees shall also be entitled to erect, construct and maintain any other machinery as the lessees may think fit and proper. All machinery brought in and erected by the lessees would remain the lessees' property and after the termination of the lease the lessees shall be entitled to remove the same provided always that the lessees shall forthwith repair and make good all damage caused to the demised premises by such removal of the lessees' machinery.
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> Clause 7 Clause 7 provides for the payment of royalty. The royalty on sugar was to be computed at the rate of Rupees Seventy-five per 100 maunds of sugar manufactured for the first five years as well as next five years then at the rate of Rupees eighty two and annas eight per 100 maunds of sugar manufactured for the third five years and Rs. 90/- for the fourth five years. The royalty on molasses was computed at three pies per maund on all molasses sold during each year of the original lease period and any renewals thereof subject to the payment of a minimum royalty of Rs. 6,500/per annum.

Clause 8 :

This clause provides that the lessee shall in addition to the royalty reserved be responsible for all the running expenses of the factory including salaries and wages and all factory staff and labour and shall pay all sugar excise duty etc. excepting the ground rents payable to the landlords and taxes on income chargeable to the lessors and shall fully reimburse the lessors in respect of such expenses which have already been incurred by the lessors since the first day of One thou- sand nine hundred and forty five and property tax.

Clause 17 :

(a)The lessors will keep the demised premises insured to the full value thereof and shall pay all expenses which will be incurred for insuring the demised premises.

(b)The lessors shall pay all expenses of running the lessors' company e.g. Directors fees, Audit fees, Ground rents etc. but not the running expenses of the factory and premises hereby demised and shall also pay for all the expenditure for additions, alterations breakdown and/or renewals and replacement of capital nature (i.e. dubitable to block account) to buildings and machineries etc. and other similar expenses of a capital nature on the demised premises.

It appears from clauses 2 and 5 that the existing machinery which was. owned by the lessor could not be removed and that the lessee would be entitled to set up additional machinery without interference from the lessor and that on the termination of the lease the lessee would be entitled to remove the same without causing any damage to the property demised. Clause 3 con-

templates that if during the period 1945-46 the lessors sell the commodity manufactured the price thereof should go back, to the lessee. Mr. Choudhury referred to clause 6 which entitled the lessee to use the railway siding during the period of the lease. But the right of use of railway siding by the lessee under this clause cannot in any way be construed as the exercise of control over the business of the assessee. The provision for minimum royalty of Rs. 65,000/- per annum indicates that the assessee had no direct interest in the production of the factory. The cumulative effect of clauses 11, 12, 13 and 14 is that the lessor will have no concern with the production of the factory which is the principal part of the business, previously carried on by the lessor. The provisions in clause 17 are that the lessors shall keep the demised premises insured to the full value and to repair and replace the machines which are of capital nature. On a scrutiny of all the clauses of the indenture of lease, our conclusion is that the intention of the assessee was to part with the entire machinery of the factory and the premises with the obvious purpose of earning rental income. It was not the intention of the assessee to treat the factory and machinery etc. as a commercial concern during the subsistence of the lease. The primary condition for the application of S. 10 of the Act is that the tax is payable by an assessee under the head "profits and gains of business" in respect of business carried on by him. When an assessee does not carry on business at all, section 10 cannot be applicable and the income that he receives cannot bear the character of profits of business. As we have already

shown there is no direct nexus between the income of the assessee and the production of the factory. The royalty payable to the assessee was not paid under clause 7 of the indenture of lease for the production in the factory. The production was only a measure of the royalty to be paid and, in any event, the measure of payment had nothing to do with the character of the payment as a receipt from business or from other sources. It follows that in the circumstances of this case the income of the assessee cannot be characterised as income from the activity of the assessee carrying on any business. The High Court was therefore right in holding that the income of the assessee was liable to be assessed under section 12 and not under section 1 0 of the Act. On behalf of the assessee reference was made to the decision of this Court in Commissioner of Excess Profit Tax, Bombay City v. Shri Lakshmi Silk Mills Ltd.(1) in which the respondent company which was formed for the purpose of manufacturing silk cloth installed a plant for dying silk yarn as a part of its business during the relevant charging accounting period. Owing to the difficulty in obtaining silk yam on account of the war it (1) 20 I.T.R. 451.

could not make use of this plant which had remained idle for some time. In August, 1943, the plant was let out to another company on a monthly rent. The question arose whether the income received by the, respondent company in the chargeable accounting period by way of rent was income from business and assessable to excess profit tax. It was held by this Court that a part of the assets did not cease to be commercial assets of that business merely because it was temporarily put to a different use or let out to another and accordingly the income from the assets would be profits of the business irrespective of the manner in which the assets were exploited by the company. But this Court clearly indicated that no general principle could be laid down which would be applicable to all cases and that each case must be decided on its own circumstances according to ordinary commonsense principles. The material facts of Lakshmi Silk Mills Ltd. (1) are that only a part of the machinery was Let out on lease and the rest of the machinery was worked by the assessee. The letting out of the machinery was for a short period of five months. There was also no letting out of the premises of the factory by the assessee. The ratio of the decision in Lakshmi Silk Mills Ltd.(1) is therefore not applicable to the present case. Reference was made on behalf of the assessee to the decision in Narain Swadeshi Weaving Mills v. Commissioner of Excess Profits Tax(2) in which the assessee firm carrying on a manufacturing business consisted of three partners, N and his two sons R & G. In April, 1940, a public limited company was incorporated with the object of taking over the business of the assessee firm. This company was director-controlled and the directors were N, his three sons R, G & S and a brother-in-law of G. The company purchased only the building and leasehold rights from the assessee firm but took over from it on lease at an annual rent the plant and machinery. The assessee firm did not thereafter manufacture anything and it bad accordingly no further trading or commercial activity. In the circumstances, it was held that letting out of the plant and the machinery by the assessee to the company could not fall within the definition of "business" under section 2(5) and as the assessee firm had, no business during the relevant period to which the Act applied, section 10A could not be invoked by the Excess Profit Tax Authorities. It was however pointed out that whether a particular activity amounts to any trade, commerce or manufacture or any adventure in the nature of trade, commerce,- or manufacture is always a difficult question to answer and no general principle ran be laid down which would be applicable to all cases and each case must be decided in the setting and background 'of its own facts. It is evident that the material facts in- the present case are somewhat different from those of Narain Swadeshi (1) 20 I.T.R. 451.

(2) 26 I.T.R. 765.

Weaving Mills' case(1) for there is no out-right sale of the building of the factory but only a lease of the factory premises together with the machinery for a long period of years.

For the reasons already expressed our conclusion is that the intention of the assessee was not to treat the factory etc. as a commercial asset during the subsistence of the lease. In other words, the intention of the assessee was to go out of the business altogether so far as the factory and the machinery was concerned with effect from 1st June, 1945 and the intention was to use the income arising from the royalty in its capacity as the owner of the factory. it follows therefore that the first question was rightly answered by the High Court in favour of the Commissioner of Income Tax. As regards the second question the argument was stressed by Mr. Choudhury that clauses (vi-a) and (vi-b) of section 10(2) are ancillary to clause (vi) and should be taken to be included within clause. (vi) as mentioned in sub-section (3) of section 12. It appears that clause (vi-a) was inserted by section 11 of the Taxation Laws (Extension to Merged States and Amendment Act, 1949). Clause (vi-b) was inserted by s. 8 of the Finance Act, 1955 with effect from 1st April, 1955. At the time of making the amendment under the said Acts, no amendment was made to section 12(3) of the Act. It was argued by Mr. Choudhury that although this was not done specifically it followed by implication that additional depreciation allowance in respect of new assets and development rebate would cornsern within the ambit of section 12(3). It appears to us that clauses (vi-a) and (vi-b) are not ancillary to clause (vi) because the scheme of clauses (vi-a) and (vi-b) is somewhat different. Clause (vi-a) which was inserted in 1949 gives additional depreciation allowance over and above the initial allowance which was formerly available under 'the second paragraph of clause (vi) in respect of buildings newly erected and new machinery and plant but not furniture installed after the 31st March, 1948. The additional allowance under this clause is confined to not more than five successive assessments falling within the period from 1st April 1949 and 31st March 1959. Further it is deductible in deter- mining the written down value, unlike the initial allowance granted under the second paragraph of clause (vi). Clause (vi-b) was inserted by the Finance Act, 1955. It grants development rebate in respect of machinery and plant provided that the machinery or plant is new and has been installed after the 31st March, 1954; and provided further that it is used wholly for the purpose of the assessee's business and the particulars prescribed for the purpose of clause (vi) have been furnished. It is manifest that clauses (vi-a) and (vi-b) introduce a new scheme (1)26 I.T.R. 765.

and cannot be treated as an integral part of clause (vi) by implication. Apart from this consideration it appears to us that these clauses were not specifically engrafted by Parliament in section 12(3) and section 12(4) while amending section 10(2) of the Act. It is therefore not permissible for the Court to read these same clauses by implication in section 12(3) and section 12(4) of the Act. The duty of the Court is to interpret the words that Parliament has used, it cannot supply the gap disclosed in an Act or to make up the deficiencies. "If", said Lord Brougham, in Gwynne v. Burnell,(1) "we depart from the plain and obvious meaning on account of such views (as those pressed in argument on 43. Geo. 3, c. 99) we do not in truth construe the Act, but alter it. We add words to it or vary the words in which its provisions are couched. We supply a defect which the legislature could easily have supplied, and are making the law, not interpreting it" (Cf. Kumar Kamalaranian Roy v. Secretary of State(2). Accordingly, we are of opinion that the assessee is not entitled to additional depreciation

and development rebate and the second question was rightly answered by the High Court in the negative. For these reasons we hold that the judgment of the High Court dated 20th September, 1963 is correct and this appeal must be dismissed with costs.

V.P.S. Appeal dismissed.

(1) (1840) 7 Cl. & F. 572, 696. (2) 66 I.A. 110,