Siddheshwar Sahakari Sakhar Karkhana ... vs C.I.T., Kolhapur & Ors on 8 September, 2004

Equivalent citations: AIR 2004 SUPREME COURT 4716, 2004 AIR SCW 5336, 2004 TAX. L. R. 1092, 2005 BOM CRSUP 229, 2004 (5) SLT 688, 2004 (7) ACE 171, (2004) 7 JT 295 (SC), 2004 (7) SCALE 519, 2004 (4) LRI 59, 2004 (12) SCC 1, 2004 (8) SRJ 439, (2004) 139 TAXMAN 434, (2004) 7 SUPREME 574, (2004) 270 ITR 1, (2004) 7 SCALE 519, (2004) 191 CURTAXREP 66, (2004) 183 TAXATION 477, 2004 (4) BOM LR 780, 2004 BOM LR 4 780

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Bench: Ruma Pal, P. Venkatarama Reddi

CASE NO.:
Appeal (civil) 6973-6975 of 2000

PETITIONER:
Siddheshwar Sahakari Sakhar Karkhana Ltd.

RESPONDENT:
C.I.T., Kolhapur & Ors.

DATE OF JUDGMENT: 08/09/2004

BENCH:
RUMA PAL & P. VENKATARAMA REDDI

JUDGMENT:

J U D G M E N T With C.A.NOs. 6976-7026, 7028-7038, 7461-7465/2000, 177- 269/2001, 7923-7924/2001, 4293/2002 and 4878/2002 AND CIVIL APPEAL NOs. 1013-1017 OF 2002 Commissioner of Income Tax, Pune Appellant Versus Shri Chatrapati Sahakari Shakar Karkhana Ltd. Respondent With C.A.Nos. 2122, 2544, 2717-2718, 2958, 3339-3348, 3429- 32, 3378-3380, 4008-09, 3996-4002, 3589-3591, 3567, 3777-3785, 3790-3796, 3962-64, 4191, 4062-63, 4666-4671, 4479-80, 4673-4682, 4732-36, 4691-4731, 4737- 4742, 5479-88, 6088-89, 5207, 5489-94, 5496-5502, 6611, 7243, 7454/2001, 466-470, 3475, 5073-77, 7399- 7400/2002, 469-470/2003 and Civil Appeal Nos. 5867, 5868, 5869, 5870, 5871-5875, 5876, 5877, 5878, 5879/2004 @ S.L.P.(C) Nos.5407, 5338, 5882, 17143/2001, 523-527, 18548, 23892/2002, 2747, 4871/2003 P. Venkatarama Reddi, J.

In all these appeals, the question for decision is whether compulsory deductions made by sugar cooperative societies on account of non-refundable and refundable deposits and other Funds are revenue receipts liable to be taxed under the Income Tax Act.

The appellants in the first batch of appeals are registered Cooperative Societies governed by the provisions of Maharashtra Co-operative Societies Act, 1960 and which is referred hereafter as 'the Act'. The affairs of these Societies are regulated by the bye-laws framed or adopted by the Societies in accordance with the procedure laid down under the Act.

The appellant in each of the appeals carries on the business of manufacturing sugar. Its members are predominantly sugarcane farmers. According to the policy of the Government, the sugarcane growing areas in the State of Maharashtra have been divided into different territorial units. Each unit has a factory for manufacturing sugar and the sugarcane growers within the territory are obliged to sell their sugarcane only to the said factory. The project cost of the appellant was met partly by share capital and partly by way of capital subsidy provided by either the Central Government (Ministry of Industrial Development) or financial institutions such as IDBI, IFCI etc. The share capital was contributed not only by the members but also by the State Government. So long as the State Government held share capital in the Society, the Government was entitled to fix the sugarcane price which it did. The bye-laws provided for deduction of amounts towards refundable and non- refundable deposits from the cane price payable to the grower members. There were also instructions of the Director of Sugars to this effect. Apart from that, pursuant to the orders passed or circulars issued by the State Government/Director of Sugars, amounts were being deducted for being credited into various Funds such as Chief Minister's Relief Fund, Y.B. Chavan Memorial Fund, Area Development Fund etc. The amounts credited to these Funds are meant to be utilized either by the Society directly as per the guidelines issued by the Director or remitted to the Government or trustees for socio-economic development of the operational area. Till the assessment year 1984-85, these collections/deposits were not treated as income of the assessee on the footing that they were not trading receipts. However, on the basis of the judgment in Bazpur Co- operative's case rendered in the year 1988, the Commissioner of Income Tax revised the assessments for the assessment years 1984-85 and 1985-86 in respect of non- refundable deposits and refundable deposits and other deductions, by exercising the power under Section 263 of the Income Tax Act. As far as the following years were concerned, namely, assessment years 1986-87, 1987-88 and 1988-89, assessment orders were passed by the Income-tax authorities treating the non-refundable deposits, refundable deposits and other deductions as trading receipts. The Commissioner of Income Tax (Appeals) dismissed the appeals filed by the assessees. All these orders were challenged before the Income Tax Appellate Tribunal by the Sugar Co-operative Societies. The matter was heard and disposed of by a special Bench of the Tribunal which decided the question in favour of the Sugar Cooperatives holding that the bye-laws in Bazpur Co-operative's case and the character of deductions made were substantially different from those in the case of Sugar Co-operatives in the State of Maharashtra. At the instance of the Revenue, the Tribunal referred 15 questions to the High Court at Bombay under Section 256(1) of the Income Tax Act. The Division Bench of the High Court addressed itself to the question whether the various amounts collected by the Society from the cane growers out of the Sugarcane Purchase Price in the name of deposits are taxable as income of the assessee Society. The learned Judges of the High Court answered the questions by holding that the non-refundable and refundable deposits are trading receipts whereas deductions on account of Area Development Fund, Cane Development Fund, Hutment Fund, Y.B. Chavan Memorial Fund, The Chief Minister's Relief Fund, Education Fund are not trading receipts and therefore not taxable. Accordingly, the References and appeals were disposed of by the High Court. The Sugar

Co-operative Societies have impugned the decision of the High Court in so far as it decided the questions raised against them and the Revenue has preferred appeals in so far as the decision went against it.

As the assessees' appeals turn much on the interpretation and implications of the bye-laws 60, 61-A and 61-B which relate to the non refundable and refundable deposits, it is worth quoting them verbatim. Bye-law No. 60: (Regarding Fixation of Cane Price) "The rate of sugarcane supplied by members will be fixed each year by the Board of Directors. The same will be of ex-gate cane. It will be the same for all the members. The Karkhana will also reimburse to the members their expenses of harvesting and transporting the cane upto the factory-gate at the rate fixed by the Board of Directors. Such transporting expenses will differ in the case of every member depending upon the distance of his field from the factory gate. Such expenditure reimbursed by the Karkhana will be treated as a part of cost of sugarcane. The Board of Directors will, each year, fix the rate of sugarcane to be paid to the members considering the constitution, objects and bye-laws of the Karkhana and the financial results of each year. However, so long as the Karkhana has not fully repaid the share capital contributed by the State Govt. and/or the loans taken on block capital account from IFC and other Central financing institutions, the Board of Directors will pay the price as fixed by the State Government.

The rate of cane supplied by the non-members at the gate will be fixed by the Board of Directors. It will not be more than the rate fixed for the Members' cane. If however, rate of cane for the non-members has to exceed the members', the approval of the State Government is necessary.

BYE-LAW NO.61-A (1) Every year the society shall collect from the members non-refundable deposits at the rate not less than Rs.1 per ton of sugarcane supplied by them. The rate of deposit will be decided by the Board of Directors. However, in determining such rate the board shall consider the amount required for the repayment of loan of I.F.C.I. and bank loan taken towards capital expenditure and the repayment of time deposits received from the members. The rate of interest on such deposit shall not exceed 12 percent so long as the Government share capital, the long term loans of IFCI, Maharashtra State Co-

operative Bank and other financial agencies advanced for capital expenditure has not been repaid. The NRD collected as above shall not be refunded to the member till the Government share capital and the term loans taken from I.F.C.I. and other financial institutions for capital expenditure are repaid fully.

(2) The Deposits collected as above shall not be refundable to the members. However, the Board may convert such deposits into shares after repayment of loans taken towards capital expenditure from Maharashtra State Co-operative Bank, Government share capital and long term loans taken from other banks for capital expenditure. The amount of fixed deposits collected by the society from members shall not exceed three times the shares held by the members. Thereafter, such fixed deposits shall not be accepted by the Karkhana. The Karkhana has to collect the deposits until it holds Government share capital and has other loans outstanding.

(3) On a member ceasing to be a member as provided in bye-law No. 22, the amount standing to the credit of his account as a nonrefundable deposit may be transferred to any other member's account at his option and approval of the board of directors or shall be refunded to such members or his legal heirs with the approval of the board of directors after the lapse of one year from ceasing to be members, on recovery of all amounts due from him if any, and after considering the financial position of the society. However, the total amount of such refund in any year shall not exceed 1/10th of the total non-refundable deposits standing at the beginning of the year.

(4) The amount of deposits so collected shall be utilized for the repayment of term loans taken for the capital expenditure as mentioned in sub-clause (2) above.

(5) The amount of deposit so collected from the members or part thereof can be transferred to the name of any other member on an application by the member. However, consent of both members in writing shall be necessary.

Bye-Law No.61-B In addition to the non-refundable deposit from the member as mentioned in bye-law No.61-A above, if the board of directors find it necessary, they shall have a right to collect the time deposits for a period not exceeding five years, out of the cane price payable to the cane supplier at a prescribed rate per ton of sugarcane supplied as may be decided by them every year. These deposits will be used by the society only for the purpose of expansion programme and capital expenditure and interest paid on these deposits will not exceed 12 percent.

Now, we shall take up the controversial issues for consideration.

Non-refundable deposits The taxability of 'non-refundable deposits' being the most contentious issue in these appeals, we shall first concentrate on that issue. At the outset, we would like to advert to the findings of the Tribunal and the High Court on this aspect.

First, we would like to setout the findings of the Tribunal in brief. The Tribunal, having noted the proposition that if a trader collects money from the customer as part of trading receipts, those receipts would constitute income, observed that the nature and object of the collection is equally material. The Tribunal observed: "what is relevant to see is not how the amount was collected but with what obligation it was collected".

After referring to the bye-laws, the Tribunal observed that the purpose for which the deductions were made in the name of non-refundable deposits was not only to pay the term loans and the Government share capital but also to convert the deposits into shares. The Tribunal pointed out that the entire amount of deposit was liable to be converted into shares except that the time at which it could be so converted was only postponed till the loans were repaid. The Tribunal pointed out that the expression 'non-refundable' only means non-refundable in cash. Though, according to the Tribunal, the collections were in the course of trading operations, it was only an occasion for the collection of the deposit and cannot be viewed as consideration for the supply of cane. The Tribunal stressed on the provision for the payment of interest and the manner in which the deposits were treated by the Society. It was stressed that the retained amounts were credited to the individual

accounts of the depositors and they were shown as liability in the balance-sheet. It means that the 'deposits' were not regarded as assessee's own money.

The Tribunal distinguished the case of Bazpur Co- operative Sugars inter alia on the ground that the amounts deducted by the Society and credited to the loss equalization fund were liable to get depleted or consumed after applying the funds for various purposes mentioned in the bye-laws including the working losses, whereas that is not the case in the present appeal.

The Tribunal summed up the position as follows:

> "To sum up, according to our understanding, the true nature and purpose of the bye-law 61A is to collect contribution towards share capital from the cane growers by deducting the amount from the sugarcane purchase price payable to them in a slow and graduated manner so that the funds so retained by the assessee could in the meantime be used for repaying the term loans taken from the financial institutions. This is a process and a method devised and adopted in such a way that the cane growers will ultimately become the shareholders contributing the necessary capital not at one time but by degrees without causing to themselves, any kind of financial strain. The incentives provided in devising the scheme are payment of interest by treating the retained money as loan in the meantime and secondly eventual conversion of the same towards share capital. Thus there is no element of income embedded in it nor can it be said that these moneys were collected or received by the assessee as and by way of income".

The REASONING OF THE HIGH COURT in support of its conclusions is summarized as follows:

> The fixation and payment of the price of sugarcane form part of the trading operations of the assessee. The deposits have been recovered by the Society as part of trading operations and therefore it constitutes "part of trading receipts". Such deductions provided a periodical return and a source of income to the Society. A reading of the bye-laws clearly indicates that the deposits are trading receipts, the primary purpose of collecting the 'deposits' being to discharge the liabilities of the society but not to issue the shares at a later point of time as held by the Tribunal. The assessee is empowered to hold on to the deposits till the repayment of the Government share capital and the loans taken from the financial institutions. In the case of deposits, a fixed maturity period is prescribed and on maturity, the depositor has a right to repayment. In the present case, there is no such period nor any such right has been given. There is no separate contract of fixed deposits between the Society and the members and no separate fund came to be created as the sums were credited to the individual accounts. The refund is within the discretion of the Board of Directors who may refuse to repay on the ground of weak financial position of Society. The payment of interest is not a conclusive factor.
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> The High Court observed:

> "In our opinion, in a matter of this type, the correct test to be applied is whether the amounts sought to be deducted reached the assessee as his income, if so, it would constitute trading receipts. On the facts of this case, it is clear that the amount reached the assessee as its income."

After referring to the case of Commissioner of Income Tax Vs. Bazpur Cooperative Sugar Factory Ltd. [(1988) 3 SCC 553], the High Court held:

> "In the present case also, under the bye-laws, the rate of deposits was fixed by the society and not by the cane growers. In the present case also, under the bye-laws, no event or contingency has been contemplated under which the share holders could demand repayment of the deposit. Hence, merely because the Karkhana has agreed to pay the interest, will not be a conclusive test to come to the conclusion that the liability has accrued to the society on deduction."

Contentions The learned senior counsel for the appellant-assessee contended that the High Court fell into error in overlooking certain important aspects of the case and laying undue stress on the fact that the amount treated as deposit is deducted from the price payable to the cane growers as part of the trading operations and, therefore, it was in the nature of trading receipt. The assessee Society was always treating the deposits as the money belonging to the members (cane growers), credited the deducted amounts to the individual accounts of the members on which interest at fixed rate was being credited. The society treated the deposits as its liability towards the members/depositors. It is contended that under the bye-laws there is sufficient indicia that the members own the deposits. For instance, in the case of resignation, the deposited amount can be claimed and in the case of death, the amount is heritable. The deposits are not utilized for carrying on the trading operations by the society, but they are utilized only for the discharge of capital liabilities. If at all, they are capital receipts, but not revenue receipts. The learned counsel further argued that it is not appropriate to describe the deposit as non-refundable deposit. It is non-refundable in the sense that it may not be paid in cash to the member, but it will go to augment the share capital of the member. With reference to some data prepared, it is pointed out that instances of refund and transfer are not rare. Justifying the findings of the High Court, it is contended by the learned senior counsel appearing for the respondent department that the true nature and character of receipt has to be taken into account notwithstanding the nomenclature used or the accounting method adopted. It is the origin or genesis of the receipt that should be taken into account but not the manner in which the amount is utilized. The fact that the deduction is from out of the price payable to the member and as a result thereof the receipts on account of deposits bring about savings in the cost of raw material is a strong indication that it is a trading receipt. It is pointed out that the members have no volition except to suffer the deduction and they have no enforceable legal rights which are otherwise available to the depositors in the ordinary course. Even in limited contingencies such as resignation and death, there is no unfettered right to get back the deposited amount lying in the account of the individual member. Even conversion into share capital is a contingency hedged in by various limitations. The discretion in this regard is vested with the Board of Directors. The Government's share capital though nominal is always retained so that the process of deduction can go on and the so called deposits are utilized for the purposes of the society. The

right to get refund of the deposit in cash or by way of conversion into share capital is, on the whole, a right which is too tenuous and remote. The learned counsel for the respondent further contended that crediting of interest is not decisive and it practically remains on paper. Placing reliance on the case of Bazpur Cooperative Sugars, it is contended that there is practically no difference between the un-amended bye-law which was considered in that case and the bye-laws in the present case. As the sheet anchor of the Department's case rests on the decision in CIT Vs. Bazpur Cooperative Sugar Factory Ltd. [(1988) 3 SCC 553], it becomes necessary to refer to that decision in detail. During the relevant assessment year 1961-62, certain amounts were deducted from the price payable for the sugarcane supplied by the members and the Society credited the same to the 'Loss Equalisation and Capital Redemption Reserve Fund'. These deductions were made under the provisions of bye-law 50. At the relevant point of time, the bye-law read as follows:

> "There shall be established a Loss Equalisation and Capital Redemption Reserve Fund in the Society. Every producer-shareholder shall deposit every year a sum not less than 32 paise and not more than 48 paise per quintal of the sugarcane supplied by him to the society as may be determined by the Board. After adjusting the losses, if any, in the working year, the deposits shall be allowed to accumulate and utilized for repayment of the initial loan from the Industrial Finance Corporation of India and thereafter for redeeming Government share.
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> The balance of the said deposit *after meeting losses shall be used in being converted into share capital in accordance with bye-law 44(xix) and each producer-shareholder shall be issued shares of the society of the corresponding value in lieu thereof."

(*emphasis supplied) The bye-law was amended with retrospective effect from 1.7.1958. The gist of the amendment is adverted to a little later.

The question arose whether the amounts received by the Society from its members by way of deduction from the price of sugarcane were revenue receipts taxable under the Income Tax Act. Before answering the question, this Court had to consider whether the amended or unamended bye-law would apply. The Court having held that the respondent-Society had no authority in law to amend the bye-law with retrospective effect as it purported to do, proceeded to examine the issue whether in the light of the unamended bye-law, the deducted amounts credited to the fund could be regarded as trading receipts liable to tax. The Court answered the question in favour of the Revenue and allowed the appeal.

It may be noticed that in contrast with the unamended bye-law, the amended bye-law contained a clear provision that the deposit into the reserve fund at a prescribed rate shall be made "until the shares to be subscribed by a Member are fully paid up". After the amounts standing to the credit of the fund are used for making partly paid shares fully paid up, the balance remaining in the account shall be liable to be refunded to the members concerned "soon after the present loan from the IFC is repaid". Thereafter, the fund shall cease to exist. There were no such definite stipulations in the unamended bye-law. However, we are not called upon to dilate on the question whether the amended bye-law would have had a different impact on the conclusion reached.

The Court reiterated the principle that "it is the true nature and quality of the receipt and not the head under which it is entered in the account books as would prove decisive" and that it makes no difference that the disputed amounts have been referred to as deposits and proceeded to consider the crucial issue in that light.

How far the ratio of the decision in Bazpur case could be applied to the case on hand is the first and foremost controversy. In the present case, the purchase and payment of price of sugarcane is undoubtedly part of trading operations of the assessee. It is in the course of such trading operations that the assessee realized the amounts (treated as deposits) with regularity and utilized the money so received in its business. To the extent the full payment is not made to the farmers, the assessee saved the raw material cost as well.

These factors may broadly satisfy the first test applied in Bazpur Cooperative Sugar's case. The following are the relevant observations in this regard:

> "It is clear that these amounts which were deducted by the respondent from the price payable to its members on account of supply of sugarcane were deducted in the course of the trading operations of the respondent and these deductions were a part of its trading operations. The receipts by way of these deductions must therefore be regarded as revenue receipts and are liable to be included in the taxable income of the respondent."

However, it needs to be clarified that the line of inquiry, in order to determine the true nature and character of the receipts, does not stop at ascertaining the mere fact whether the realization was in the course of trading operations. The moment it is found that certain amounts were deducted by the assessee out of the price payable to its members who supplied the raw material, the conclusion does not necessarily follow that all such realizations get impressed with the character of revenue receipts, giving rise to taxable income in the hands of the assessee. It is not any and every receipt linked to the trading activity that acquires the quality of revenue receipt. The tribunal or the court should go further and delve into the true nature, character and purpose of the realizations. If the amounts are meant to be held as deposits liable to be returned to the depositor at a specified point of time or on the happening of specified contingencies which are by no means uncertain or is otherwise treated as members' money the depository having no unfettered dominion over the said funds, then, it is difficult to characterize them as the income of the assessee. The realization of monies from the grower- members in the course of trading operations could as well be construed to be an occasion, mode or convenient point of time at which the 'deposit' could be collected. Perhaps keeping this legal position in view, notwithstanding what has been stated in the earlier portion of the judgment, the learned Judges proceeded to address the next question, i.e, whether the receipts by way of deductions could be regarded as deposits as described in the bye-laws. While answering that question in the negative, the Court pointed out that it is the true nature and quality of the receipt that is material but not the head under which it is entered in the account books a principle which is reiterated in a catena of decisions. The Court then went on to conclude that the receipts by way of deductions from the purchase price were not in the nature of deposits. In this context, the reasoning of the Bench may be noticed.

> "The essence of a deposit is that there must be a liability to return it to the party by whom or on whose behalf it is made on the fulfillment of certain conditions. Under the amended (sic unamended) by-law, the amounts deducted from the price and credited to the said fund were first liable to be used in adjusting the losses of the respondent society in the working year;
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> thereafter in the repayment of initial loan from the Industrial Finance Corporation of Indian and then for redeeming the government share and only in the event of any balance being left, it was liable to be converted to share capital. The primary purpose for which the deposits were liable to be used were not to issue shares to the members from whose amounts the deductions were made but for the discharging of liabilities of the respondent-society. In these circumstances, the receipts constituted by these deductions were really trading receipts of the assessee society "

The Court apparently felt that the event of return of the amounts by way of conversion into share capital was remote, if not impossible. In meeting the point urged by the assessee that it was a deposit, the Court proceeded to apply the primary purpose test. The primary purpose, according to the learned Judges, was not to issue shares to the members but it was meant to discharge various liabilities of the society. Therefore, it was felt that it would be a misnomer to call it members' money or a returnable deposit. That is the ratio of the decision. To what extent the principle laid down or the test applied in the Bazpur case can be pressed into service in the present case is the question which needs our close attention. There are two distinguishing features which become apparent on a reading of the bye-laws. The first is the absence of provision for payment of interest under the bye-laws of Bazpur Co-operative Sugars Ltd. Secondly, in Bazpur case the deducted amounts credited to "loss equalization and capital redemption reserve fund" are liable to be adjusted against the losses of any working year. It is only after adjusting such losses, the deposits are allowed to accumulate and be utilized for repayment of IFCI loan and for redeeming the Government's share contribution. In the process of such adjustment, the entire amount collected from the members and credited to the fund may be dissipated or consumed, whereas in the instant case, the amount collected as deposit remains intact, though it could be utilized from time to time for meeting certain liabilities of capital nature. However, there is one qualification in this behalf. If the society has not incurred any loss and it remains a profit-making concern, the situation will be very similar in both the cases. The amounts will then be utilized for repayment of long-term loans due to the financial institutions and the Government's share capital and after such process of repayment is complete, the disputed amounts could be made available to the grower members in the form of increased shares. Yet, in Bazpur case, at the time the sums were received from the grower-member and remitted to the loss equalization fund, there was no knowing whether the 'deposit' would remain in tact at all. The claim of the member to the deposited amount at that stage was too tenuous and slippery to earn the legal recognition of any proprietory interest over it. It cannot be said that the member had the right to get back the amount when it was recovered and credited to the Fund. The ultimate conclusion reached in Bazpur case can be explained on this basis. There is yet another angle from which the problem can be viewed. As between the member and the society, who is having substantial dominion over the 'deposits'? In Bazpur case the answer could only be that it is the assessee-society which had such dominion. The position is different in the present case, as explained

hereafter.

The ratio in Bazpur case not being squarely applicable, the whole basis on which the revision was initiated crumbles. Still, we have to examine whether the assessment of impugned amounts as taxable income is justified in law.

Keeping in view the bye-laws of the society, the approach of this Court in Bazpur case and the settled principles, we must examine the fundamental question, viz., what is the true nature and quality of the receipts sought to be taxed? The question has to be examined from various angles running in a common direction. For instance, it becomes necessary to enquire: Do the receipts bear the character of income at the time they reach the hands of the assessee? Does the title to the money get vested with the assessee Society once and for all, the assessee exercising complete dominion over the funds in question? OR, is it to be regarded as the money of depositors/members notwithstanding the custody of the Society and the authority given to the Management of the Society to utilize the money for the overall advantage of the Society? Does the assessee- Society stand in the position of debtor in relation to these deposits? Is there in law an obligation to repay the amounts, i.e, by way of augmentation of share capital of members? What is the primary purpose behind the collection of the amounts as deposits? These are the various questions of overlapping nature which have been debated before us in some form or the other, and call for answers in order to resolve the crucial controversy. Though the manner in which the sums are treated by the assessee in its accounts is neither conclusive nor a sure indication of the nature and character of the receipt, yet, it is not an irrelevant factor. As rightly observed by the High Court, the relevant bye- laws of the Society shall be kept in the forefront in finding an answer to the issue raised. On an analysis of the relevant bye-laws regarding sugarcane price and non-refundable deposits, the following salient features are discernible:

1. The price of sugarcane is fixed every year by the Board of Directors, on a consideration of relevant factors.

2. However, so long as the share capital contribution of the State Government and/or the loans taken on capital account from IFCI and other Central Financial Institutions remain outstanding, the price as fixed by the State Government is liable to be paid by the society.

3. Every year the society shall collect from the members supplying sugarcane a non-refundable deposit at the minimum rate of Re.1/- per ton. In fixing the rate, the Board of Directors has to take into account the liabilities towards the loan due to IFCI and other loans borrowed for capital expenditure and the repayment of time deposits received from the members.

4. The Society should continue to collect the deposits so long as it holds Government share capital and other loans (on capital account) are outstanding. However, the deposits collected by the Society shall not exceed three times the shares held by the members.

5. The rate of interest on the deposits collected shall not exceed 12%.

6. The non-refundable deposit shall not be refunded to the members till the Government share capital and term loans taken from IFCI etc. towards capital expenditure are repaid fully. On such repayment, the Management of the Society may convert such deposits into shares.

7. The amount of deposits collected shall be utilized for the repayment of term loans taken for the purpose of capital expenditure.

8. The amount collected as deposit can be transferred to the name of any other member on an application submitted in this behalf.

9. On ceasing to be a member for whatsoever reason, the non-refundable deposit standing to his credit may be transferred to any other member's account subject to the approval of the Board of Directors or can be refunded to such member or his legal-heirs with the approval of the Board of Directors, but, such refund can only be granted after the lapse of one year, that too after considering the financial position of the Society.

Although the use of the expression 'deposit' does not conclude the issue, there are intrinsic indications in the bye-laws that the expression has been used to mean just what it says. These are: (a) conversion of the deposit into additional shares, (b) transferability / heritability, (c) refundability and (d) payment of interest on the deposit. The first three features are no doubt dependent upon occurrence of certain contingencies or hedged in by certain limitations. But the deposited amount is not denuded of its character of 'deposit' for that reason alone. First, discussion needs to be focused on the first feature, namely, conversion of deposit into shares. The Tribunal rightly pointed out and it is not disputed before us that such conversion is as good as refund. Such conversion into additional shares is however postponed till the events of repayment of loans towards capital expenditure and the repayment of Government share capital happen. In other words, till such time, the member / depositor has no immediate right to demand the payment. Nevertheless, the obligation to repay stood annexed to the deposited amount at the time it was received by the assessee subject of course to the occurrence of the contingency specified in the bye-law itself. It cannot be said, as has been said by the High Court, that "under the bye-laws, no event or contingency has been contemplated" under which the members could demand the repayment of the deposit. Nor can it be said that even after the happening of the event specified in the bye-laws, the right to demand repayment becomes illusory in view of the discretion reserved to the Board of Directors of the Society. In this context, much of the argument has been built up on the use of the expression 'may' followed by the words "convert such deposits into shares after repayment of loans etc." It is contended by the learned counsel appearing for the Revenue that the Board of Directors may very well refuse to convert the deposits into shares in exercise of its discretion on the ostensible ground that the financial position of the Society does not permit such conversion. The very existence of discretion, it is pointed out, negates the existence of liability to convert the deposit into shares. We cannot accede to this contention. Once the loans of the description mentioned in the bye-laws

which were outstanding on the date the deposit was made are repaid, in our view, the Board of Directors is bound to convert the deposit amount into shares. The discretion is always coupled with a duty; the discretion cannot be used to circumvent the obligation cast under the law or contract governing the parties. In our view, it would be appropriate to read the expression 'may' as 'shall'. On the occurrence of the specified event, namely, the repayment of the loans referred to in the bye-law and the Government share capital, the member/depositor can clutch at a legally enforceable right to demand repayment, may be, in the form of conversion into additional shares. In our view, the retention of the deposited money with the Society in order to utilize the same for repayment of term loans etc., does not denude the amount of its character of 'deposit' carrying with it the obligation to repay. Nor is it necessary, as the High Court was inclined to think, that the separate identity of the deposited amounts should be kept up. The absence of the right to secure repayment on demand is again not inconsistent with the receipt being a deposit. Liability to return need not be immediate and unconditional, following a demand by the depositor. Even if such liability gets crystallized on the happening of a specified contingency, it is still a liability which can be legally enforced by the depositor. The existence of such liability is an antithesis to the idea of ownership of the money by the Society.

Deposits are of various types with variations in their features and incidents. It would be apposite, in this context to refer to certain passages dealing with deposits from well known treatises. In Corpus juris secundum (volume -26A) the following passages occur:

> The deposits are classified as Special Deposits, General Deposits and other Deposits.
>
> Special Deposit:
>
> A special deposit is one in which the identical subject matter deposited must be kept and redelivered, or applied to a particular purpose.
>
> General Deposit:
>
> A general deposit is one in which the identical subject matter need not be returned and, as distinguished from a deposit for safe-keeping, this form of deposit has been termed a deposit for exchange, that is, one in which the depositary is only bound to return a thing corresponding in kind to that which is deposited. In determining whether or not a deposit is special, the character of the business of the depositary is entitled to considerable weight, but is not controlling.
>
> It is further stated:
>
> "An agreement to pay interest is strong evidence that a deposit is general rather than special".
>
> Dealing with duties and liabilities of depository it is stated:

"An obligation to redeliver the subject matter in specie or in kind, on the demand of the depositor or otherwise in accordance with the terms of the deposit*, is necessary to constitute the transaction a deposit, and it is the duty of the depositary to make delivery in accordance therewith. The fact that there is not to be a redelivery of the thing delivered is a strong indication that the transaction is not a deposit. In the absence of an agreement to the contrary, the depositary must also return with the thing deposited all increase which has accrued thereto during the term of the deposit. The fact that the depositor has the right to sell or exchange the deposit and substitute therefor the proceeds of the sale or exchange does not deprive the deposit of its character as such".

(*emphasis supplied) In words and phrases (Permanent edition, Volume-39A), the distinction between the special deposit and the general deposit and the concept of a specific deposit is clarified as follows:-

"The distinction between a 'special deposit' and a 'general deposit' is generally held to be that the subject of a 'general deposit' is mingled with the general assets of the depository, whose property it becomes, and its separate identity is lost, and the relation between the bank and the depositor is that of debtor and creditor; while the subject of a 'special deposit' is to keep safely, separate and distinct from the general assets of the bank, as the title remains in the depositor, who is entitled to receive back the identical thing deposited, and the relation assumed between the depositor and the bank is that of bailor and bailee". "Money deposited for a definite purpose without any agreement or understanding that it shall not be used by the depositee for its own purposes is a 'general deposit for a specific purpose', or, as it is sometimes called, a 'specific deposit' and creates the relation of debtor and creditor just as in the case of a general deposit". (emphasis supplied) In Shanti Prasad Vs. Director of Enforcement [(1963) 2 SCR 297] this Court, while dealing with the deposit in a bank, reiterated the settled law that relationship between the banker and the customer is one of debtor and creditor and observed thus:

"The banker is entitled to use the monies without being called upon to account for such user, his only liability being to return the amount in accordance with the terms agreed between him and the customer." (emphasis supplied) The above juristic exposition of the concept of deposit removes the possible doubts on the impugned amounts being treated as deposits.

It is the contention of the learned senior counsel appearing for the Revenue that the possibility of return of the deposit (by way of conversion into shares) depends on uncertain events and the repayment remains to be a remote possibility. It is difficult to appreciate this contention. True, the obligation to refund the deposit by way of conversion into shares would arise only on the occurrence of the contingencies specified in the bye-laws. But, in our view, it is wrong to assume that the events giving rise to refund are uncertain. The repayment of loans taken for capital

expenditure and the share capital of the Government are the two specified events which are by no means uncertain, though the time of repayment is indefinite. On the occurrence of the said two events, the right to demand refund would accrue to the depositor. The obligation which had been in inchoate form ripened itself into a complete obligation on the occurring of specified events stipulated in the bye laws. Such an obligation may be contingent in nature initially but the right to enforce the obligation inheres in the depositor from the beginning. The existence of other features such as transferability of the deposit to another member and the provision for refund of the deposited amount to the member in case of cessation of membership or to his legal heirs in case of death, are important indicators against the treatment of the deposited amount as the money belonging to the Society. The payment of interest from year to year at a specified rate is another important factor that supports the conclusion of the disputed sum being a deposit. Such payment of interest is only consistent with the fact that the deposited amount still belongs to the member. The fact that the deposited amounts are credited to the individual accounts of the members is a corroborative circumstance to indicate that the deposits belong to the members.

In Commissioner of Internal Revenue Vs. Indianapolis Power & Light Company [493 US 203], the question arose whether the deposit amount was an advance payment towards electricity charges and therefore liable to be subjected to income-tax. While recognizing the principle that the loan proceeds do not qualify as income because of the repayment obligation, the US Supreme Court applied the test whether the assessee enjoyed complete dominion over the customer deposits entrusted to it and observed thus:

" .IPL hardly enjoyed 'complete dominion' over the customer deposits entrusted to it. Rather, these deposits were acquired subject to an express 'obligation to repay', either at the time service was terminated or at the time a customer established good credit. So long as the customer fulfills his legal obligation to make timely payments, his deposit ultimately is to be refunded, and both the timing and method of that refund are largely within the control of the customer."

In that case too, the refund was linked to contingent events which were not uncertain.

Applying the above test to the present case, we cannot hold that the assessee-Society had absolute dominion over the impugned deposits. Firstly, the manner of user of the deposit is limited by the bye-laws. Para (4) of bye-law 61-A makes it clear that the amount of deposits shall be utilized for the repayment of term loans taken for the capital expenditure from the banks and financial institutions. Unlike the case of Bazpur Co-operative Society the deposited amount cannot be 'adjusted' against the term loans much less the losses though it can be temporarily utilized by the assessee to clear the loans. The fact that the depositor can seek transfer of the deposit to another member by filing an application for that purpose again highlights the fact

that the power of disposal of the deposit lies with the member. The obligation to convert the deposits into shares subsequent to the repayment of certain types of loans coupled with the right given to the member to seek transfer of the amount lying to his credit and the obligation to refund the deposit to the depositor on cessation of his membership or to his legal heirs in case of death subject of course to certain restrictions, are all pointers that the assessee can exercise dominion over the deposits only in a limited sphere. On a consideration of the bye-laws as a whole, it is difficult to hold that either the assessee or the depositor exercises complete dominion over the deposited amounts. If so, it is not possible to countenance the plea that the title to the deposits will throughout remain in the hands of the Society and the depositor has no stake or interest therein, once it reaches the assessee's hands.

Viewed from the point of view of the primary purpose of deposit a test which has been formulated by this Court in Bazpur case though without much of discussion, we are of the view that the answer cannot be the same as in Bazpur case. In this connection the Tribunal recorded the finding that the purpose of collecting non-refundable deposits "was not only to repay term loans taken from financial institutions and to repay the government share capital, but also to convert the so called deposits into shares". The Tribunal expressed the view that the whole idea was to increase the capital base of the assessee in a phased manner by retaining some portion of the money payable to cane-growers, while at the same time compensating the depositors by way of interest. However, the High Court was not inclined to accept the finding of the Tribunal. The High Court commented:

" on the contrary the above bye-laws clearly indicate that the primary purpose of collecting the deposits i.e. the deductions was to discharge the liabilities of the Society".

We are unable to endorse the view taken by the High Court. Meeting the financial commitments of the Society may be one of the purposes for which the deposits were collected but that is not all. The augmentation of the share capital which may be in the overall interests of the members as well as the Society is an equally important purpose which cannot be overlooked. At any rate, the view taken by the Tribunal appears to be a reasonable view and the High Court need not have disturbed that finding.

The High Court relied on the decision of the same High Court in Shree Nirmal Commercial Ltd. Vs. C.I.T. [193 in ITR 694] in order to hold that the payment of interest on the deposited amount is not inconsistent with the amount being a revenue receipt. We are of the view that the ratio of that decision cannot be pressed into service in the present case. On a consideration of the Scheme and Agreement under which non-refundable interest-bearing deposit was collected by the assessee-company, it was found as a matter of fact that "the deposit was the absolute property of the Company and the provision for payment of interest was only a device

for showing the amount received in the course of trade as deposit." In the instant case, the plea of device, though raised faintly before the Tribunal, was not accepted. It rejected the argument that the provision in the bye-law 61-A providing for conversion of deposits into share-capital was a make believe affair and that the High Court in answer to question No.12 affirmed this finding. To fortify the argument that the disputed amount is not the income of the assessee, the learned Sr. Counsel appearing for the assessees pointed out that the entire amount of cane price was treated as agricultural income of the member and was taxed accordingly under the Maharashtra Agricultural Income Tax Act. So also, the interest payable on the deposits was shown as the member's income and the deposits were shown in the wealth tax returns as the member's wealth. According to the learned counsel, all this indicated as to how the deposited amounts were being treated by the members apart from the assessees. We are not inclined to delve into these aspects which are being projected for the first time before us. Though this stand was taken before the Tribunal and a sample assessment order was filed, evidently the finding of the Tribunal was not invited on this aspect. The learned counsel for the Revenue tried to invoke Section 41(1) to fortify his argument that the impugned receipts constitute income in the hands of the assessee Society. No such question was considered by the High Court or even by the Tribunal specifically. In fact, the questions formulated in the reference cases indicate that the decision of the High Court was not invited on this point. Hence we do not propose to deal with it.

As regards refundable deposits, the relevant bye-law is 61-B which has been quoted supra. In the light of what we have said about non-refundable deposits, it does not require further elaboration to conclude that these deposits cannot in any sense be treated as income of the assessee- Society. Though deducted from the cane price, they are pure and simple fixed deposits repayable on the expiry of a definite period of time with interest. The restrictions and conditions governing the non-refundable deposits are not incorporated in bye-law 61-B. These 'deposits' are akin to the transaction of loan. They are clearly liable to be excluded from taxable income.

There is one more point to be adverted to. Compulsory nature of the deposit has been stressed by the Revenue and the High Court too as being obnoxious to the idea of a deposit. It has been pointed out that the member had no option but to agree for deduction on pre-ordained terms and there could not be in law a contract creating deposit. This contention, however, does not appeal to us. A person by becoming the member of a Co-operative Society, volunteers to abide by the bye-laws of the Society, the real object of which is to provide for internal management of the Society including rendering assistance to the members. There is an authority for the proposition that the bye-laws of the Co- operative Society constitute a contract between the Society represented by its managing body and its constituents. This legal position has been recognized in Hyderabad Karnataka Education Society Vs. Registrar of Societies and Others [(2000) 1 SCC 566] (vide paragraph 28). In The Cooperative Central Bank Ltd. & Ors. Vs. The Additional Industrial Tribunal, Andhra

Pradesh [(1969) 2 SCC 43], this Court held that the bye-laws of the Society framed by virtue of the authority conferred by the Co-operative Societies Act were on par with Articles of Association of a Company, which, it is well settled, establish a contract between the Company and its members and between the members inter se (vide paragraph 14 in N.C. Sanyal Vs. Calcutta Stock Exchange Association Ltd. [(1971) 1 SCC 57]). That apart, the mere fact that the contract has to be entered into in conformity with and subject to restrictions imposed by law does not per se impinge on the consensual element in the contract. "Compulsion of law is not coercion" and despite such compulsion, "in the eye of law, the agreement is freely made", as pointed out in Andhra Sugars Ltd. Vs. State of A.P. [AIR 1968 SC 599].

For the aforesaid reasons we conclude that the non- refundable and refundable deposits cannot be treated as the income of the assessee-Societies. The Civil Appeals filed by the assessees/Co-operative Sugar Factories are allowed without costs.

Revenue's appeals Re : Other deductions made towards various Funds Leave granted in Special leave petition (Civil) Nos. 5407, 5338, 5882, 17143 of 2001, 523-527, 18548, 23892 of 2002, 2747 and 4871 of 2003.

Pursuant to the instructions issued and the guidelines evolved by the Director of Sugars, may be under the authority of the State Government, the deductions at the prescribed rate were made out of the cane price for being credited into (1) Chief Minister's Relief Fund, (2) Late Shri Y.B. Chavan Memorial Fund, (3) Hutment Fund, (4) Area Development Fund, (5) Cane Development Fund and (6) Members' Small Savings Fund. It is common ground that the identity of such deducted amounts was being preserved and separate accounts were being maintained in relation thereto. In regard to Area Development Fund, the Tribunal was of the view that the assessee had no control over these funds and they were collected on behalf of and as an agent of the State Government. In regard to other funds, the Tribunal held that the deducted amounts were only retained with the assessee in order to make them over to the Government which ultimately spent the same for certain purposes. The High Court, while pointing out that "a trading receipt means the assessee's own money which can be put to any use", applied the principle of diversion of income by overriding title. The High Court concurred with the conclusion of the Tribunal.

Unfortunately, in none of the orders of the Income Tax authorities or the Tribunal, the details relating to the nature and purpose of the funds and the manner of disbursement of the amounts have been set out though there is only a skeletal reference here and there. That is why perhaps the High Court too could not give these factual details in its order. Even in the appeal memorandum or the written submissions filed on behalf of the Revenue we do not find these details. Despite this handicap, we have looked into some of the orders and circulars issued by the Director of Sugars and other authorities contained in the paper book submitted to the Income Tax Appellate Tribunal.

As regards the Chief Minister's Relief Fund, Late Y.B. Chavan Memorial Fund and Hutment Fund, no serious attempt has been made to assail the order of the Tribunal/High Court, the obvious reason being that they were required to be and in fact being remitted to the Government or to the Trustees of late Y.B. Chavan Prathisthan. The assessee merely acted as an agent in collecting the amounts and remitting the same to the Government/Trustees. In truth and in substance, the money collected by the assessee was not reaching the assessee as part of its income, but the collection was made "for and on behalf of the person to whom it is payable", to borrow the language in CIT Vs. Sheetal Das [41 ITR 367]. It had no manner of right or title over the said monies. The amount collected towards Hutment Fund stands on no different footing. It was meant to be handed over to Collector for the purpose of providing shelter to landless poor inhabitants within the area of operation of the sugar factory. We agree with the conclusion reached by the Tribunal and the High Court that these receipts should not be treated as income of the assessee.

The main contest by the Department has been in respect of Area Development Fund and Cane Development Fund. The Tribunal has also dealt with these items separately at paragraphs 28 & 29.

The Area Development Fund, as we see from the various communications placed in the paper-book, is meant to enable the co-operative sugar factories to render socio-economic services in the area of operation. The area development programmes may cover agricultural extension, irrigation facilities, educational and medical services, development of animal husbandry and poultry, drought relief work and so on. By doing so, the sugar cooperatives will be supplementing the efforts of the Government in promoting the socio-economic development of the area. The Board of Directors of the cooperative society are required to pass a resolution specifying the details of expenditure proposed to be incurred from out of the Area Development Fund. They should obtain the sanction of the Director of Sugars for incurring such expenditure. Such information is also required to be placed before the General Body of the society and the approval to be obtained from the General Body. On 21st June, 1988, the Agriculture and Co-operation department of the Government of Maharashtra framed certain directive principles laying down the modalities of utilization of Area Development Funds. The said order was issued in exercise of the power under Section 79-A of the Maharashtra State Cooperative Societies Act. This order passed during the middle of the last assessment year relevant to these appeals gives statutory basis for the already existing practice. It is difficult to equate this fund to the other categories of funds, as has been done by the Tribunal and affirmed by the High Court. Unlike the other funds like Chief Minister's Relief Fund, the amount collected towards Area Development Fund is retained by the sugar factory itself and utilized as per the guidelines issued by the Government or the National Cooperatives Development Corporation. The collective Body of the Society and its elected representatives take the decision as to how much amount has to be spent and for what purposes. The Director of Sugars or other designated official, no doubt acts in a

supervisory capacity to oversee that the funds are properly utilized. On that account, it cannot be said that the collection is made by the Society as an agent of the Government or the proprietary interest in the funds is vested with the Government. The conclusion has been reached by the Tribunal mainly on the basis of requirement of prior sanction of the Director of Sugars for incurring the expenditure. Such restriction prescribed in the larger interest of the Society itself does not in any way detract from the fact that the Societies concerned do exercise dominion over the fund and deal with that money subject of course to the guidelines and restrictions evolved by the Government. The Tribunal failed to approach the question in proper perspective on an analysis of the relevant circulars and orders. The High Court too fell into an error in invoking the theory of diversion of income at source. The crux of the matter is that there has never been a diversion of income to a third party (Government) before it reached the assessee. The receipts in the form of Area Development Fund always remained with the assessee.

It could still be contended, as has been contended by learned senior counsel appearing for the assessees, that the realizations made by the assessee towards Area Development Fund are impressed with a specific legal obligation to spend the monies for specified purposes which are unrelated to the business of the sugar factory and therefore such receipts cannot be treated as income of the assessee. The analogy of collection of amounts towards charity, as in the case of C.I.T. Vs. Bijlee Cotton Mills [(1979) 1 SCC 496], has been invoked to substantiate the argument. It is contended that the realizations towards Area Development Fund would more or less stand on the same footing as deposits. The controversy has not been approached in the light of the above arguments. We do not consider it appropriate to express our view for the first time, especially when the determination thereof may depend on the consideration of certain facts. We therefore leave this point open for fresh determination by the Tribunal.

As far as Sugar Cane Development Fund is concerned, the case of the Revenue seems to stand on a stronger footing. In the paper-book, we find a Circular dated 18th August, 1986 in which certain directive principles have been laid down to regulate the expenditure to be incurred out of Cane Development Fund. The items specified in the directive principles are (1) green manuring, (2) lift irrigation schemes, (3) distribution of cane seeds and (4) construction of new wells or deepening of old wells. The sugar factory is required to make sure that any project which they want to undertake out of the Cane Development Fund is technically and financially sound and to send the proposals in advance to the Directorate of Sugar for requisite sanction. The projects will directly benefit the members and augment the sugarcane production which will incidentally help the Society in its manufacturing operations. The beneficiaries under the scheme are no other than the members of the Sugar Cooperative Society concerned and the advantage of enhanced production of sugarcane will ultimately be felt by the Society itself. Unlike the Area Development Fund, the monies out of Cane Development Fund are not spent for purposes

unconnected with the growth and functioning of the sugar factory. The Tribunal was inclined to view it as a 'compulsory levy' on the depositors collected by the Government through the agency of sugar factory. This approach in our view is wholly unsustainable and is in the realm of surmise. We do not also see any scope for the application of principle of diversion of income at source in the case of collections made towards Cane Development Fund. The amounts realized on this account undoubtedly reach the assessee as its income and is utilized by the assessee for the benefit of itself and its members. As already observed, the supervisory role of the Directorate of Sugar to ensure that the amount is properly utilized to promote the objectives with which the fund was formed, does not make a material difference on the quality and character of the receipt. We are therefore of the view that the deductions made out of cane price towards Cane Development Fund should be treated as the income of the assessee. We are, of course, not expressing any view whether it is a permissible deduction under the provisions of the Income Tax Act. If any such claim is made, the Tribunal shall examine the same when the matters are taken up by it to consider the issue of tax liability in relation to Area Development Fund. Though the item relating to collections towards Members' Small Savings Scheme has also been included in the memorandum of appeal, no argument has been advanced on this aspect and therefore we need not deal with this.

We therefore allow the appeals of the Commissioner of Income Tax partly in respect of the amounts collected by the respondent-Societies towards Cane Development Fund and Area Development Fund. We declare that the amount collected towards Cane Development Fund shall be treated as the income of the assessees and any claim for deduction shall be entertained and decided by the Tribunal. As regards the Area Development Fund, the matters are remitted to the Income Tax Appellate Tribunal, Pune Bench for fresh determination subject to the observations made in this judgment. In respect of other items, the appeals shall stand dismissed.

In the ultimate analysis, the assessees' appeals are allowed and the Commissioner's appeals are partly allowed to the extent indicated above.