P. H. Divecha And Another vs Commissioner Of Income-Tax,Bombay I on 11 December, 1962

Equivalent citations: 1964 AIR 758, 1963 SCR SUPL. (2) 949, AIR 1964 SUPREME COURT 758

Author: M. Hidayatullah

Bench: M. Hidayatullah, S.K. Das, J.L. Kapur, A.K. Sarkar, Raghubar Dayal

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           PETITIONER:
P.   H. DIVECHA AND ANOTHER

        Vs.

RESPONDENT:
COMMISSIONER OF INCOME-TAX,BOMBAY I

DATE OF JUDGMENT:
11/12/1962

BENCH:
HIDAYATULLAH, M.
BENCH:
HIDAYATULLAH, M.
DAS, S.K.
KAPUR, J.L.
SARKAR, A.K.
DAYAL, RAGHUBAR

CITATION:
 1964 AIR  758            1963 SCR  Supl. (2) 949
 CITATOR INFO :
 R          1971 SC1590  (9)
 R          1973 SC 524  (4)
 E          1992 SC1495  (14,31)


ACT:
Income   Tax-Firm   of  three  partners-Agreement   with   a
company--creates  monopoly  to sell  and  deliver  company's
bulbs in favour of the firm-Undertaking by firm-To sell only
company's  bulbs-Agreement  operates  16  years-Failure   of
negotiations for reneuul-Transition agreement-Company agrees
to  pay  Rs.  40,000/- per annum to each  partner  during  3
years-Assessment  year-Each  partner receives  Rs.  10,000/-
-Whether trading asset or Capital assets-Compensation or  ex
gratia payment.
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HEADNOTE:
The two appellants along with another were carrying on business in Electrical goods under the firm name Precious Electric Co. In 1938 this firm entered into an agreement with M/s. Phillips Electric Co. (India) Ltd. The material terms of the agreement were the following. The firm was to have an exclusive territory for sale of Phillips bulbs and undertook to sell only Phillips bulbs in the territory. The agreement allowed the firm compensation if Phillips bulbs were sold in the territory by the company. The agreement was terminable by a three months notice on either side. There was no stipulation in the agreement as to the quantity or quality of bulbs to be bought by the firm, neither was it agreed that the firm was to act as an agent of the company. The agreement continued for 16 years. In 1954 negotiations for a fresh agreement were conducted but they were not successful. Since the company was taking over the business of selling the bulbs in the territory a working scheme for the transition period following the termination of the agreement was reached. The most material term of the scheme was that the company would pay Rs. 40,000/per annum as a gesture of goodwill in quarterly instalments to each of the partners during a period of three years from the date of the expiry of the existing agreement. In the assessment year each of the partners received two quarterly payments of Rs. 10,000/- each. This amount was taxed by the Income Tax Officer in respect of the two appellants under s. 10 (5A) of the Indian Income Tax Act, 1922. The appellants appealed without success to. the Assistant Commissioner. Thereupon
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they appealed to the Tribunal contending that the amount assessed was compensation paid for the termination of the agreement or it was an ex gratia payment. It was further contended that the payment made to the individual partners did not constitute a receipt of the firm's business. Alternatively it was argued that the said receipt was not liable to be included in the total income of the receipients by reason, of s. 4 (3) (VI I) of the Income Tax Act. The Tribunal did not accept any of these contentions but it referred three questions for the decision of the High Court. These questions were whether the receipt in question was a taxable receipt, if so whether it was liable to be not 'included in the total income under s. 4 (3) (VII) and whether the said receipt fell within s, 10 (5A) (d). The High Court answered that the receipt was a taxable receipt and s. 4(3)VII did not exempt it from liability. The third question was left unanswered. The present appeal has arisen byway of a certificate granted by the High Court.
The contentions were that the agreement was not a trading agreement; it constituted an asset on the termination of which compensation was paid to make up for the loss of this

capital asset; in the alternative that even if it was not compensation for loss of capital it was an ad hoc ex gratia payment in the nature of `solatium' as described by the Privy Council in Income-tax Commissioner v. Shaw Wallace & Co. (1932) L. R. 59 1. A. 206. For the respondent it was contended that since there was no premature termination of the agreement even if it is treated as capital, it has exhausted itself and therefore must be treated as revenue from other sources' under s. 12 of the Act.
Held, that in determining whether a payment amounts to a return for loss of a capital asset or is income, profit or gain liable to income-tax, one must have regard to the nature and quality of the payment. If the payment was not received to compensate for loss of profits of business the receipt cannot properly be described as income, profit or gains. The size of the amount paid or the periodicity of the payments have no decisive bearing on the matter.
The Commissioner of Incone-tax v. Vazir Sultan & Sons., [1959] Supp. 2 S. C. R. 375, Godrej & Co. v. Commissioner of Income-tax.-[1960] I S. C. R. 572, Commissioner of IncomeTax v. Jairam Yalji, [1959] 36 I.T.R. 148 and Senainam Doongar Mal v. Commissioner of Income-tax, [1 961] 42 I.T.R. 392, referred to.
The payment cannot be connected with estimated loss of profits since, the terms of the agreement show that the firm
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was not entitled to be compensated for temporary suspension of the benefits or a complete termination of those benefits.
Glenboig Union Fireclay Co. Ltd. v. Commissioner of Inland Revenue, (1922) T.C. 472, referred to.
In the absence of any proof that the amount paid was the likely profit it is difficult to say that the payment replaced those profits.
The agreement in the present case was not an agreement for the purchase of bulbs. It mentioned no quantity or quality or price. It only secured to the firm a right to exclusive purchase of bulbs for sale in an exclusive territory. The agreement can only be described as an agreement which constituted a source and a monopoly and which gave an enduring advantage to a trader in his trade. The loss of such an agreement must be regarded as falling on the capital side and not in the course of his ordinary trading. If the agreement had been breached prematurely the damages would not have been calculated on the basis of outstanding contracts only but on the basis of an a vantage lost.
Bush Beach & Gent Ltd. v. Road. (1939) 22 T.C. 519 Short Bros. Ltd. v. Commissioner of Inland Revenue, (1927) 12 T.C. 955, Commissioner of Inland Revenue v. North Fleet Coal and Ballast Co. Ltd., [1927] 12 T.C. 1302 and Yen Den Berghs Ltd. v. Clark, (1935) 19 T. C. 390, referred to.
Even if the payment cannot be considered as a payment for loss of capital it cannot be regarded as payment for any services rendered or likely to be rendered. It was an ad

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hoc  payment  out of gratitude and in  appreciation  of  the
personal qualities of the assessees.
Chibbett  v.  Joseph  Robinson & Sons,  (1924)  9  T.C.  49,
referred to.
The  receipt not being income profit or gain s. 4 (3)  (VII)
had no application.
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JUDGMENT:

CIVIL APPELLATE JURISDICTION : Civil Appeal No. 332 of 1961. Appeal from the judgment and ordered dated June 23, 1959, of the Bombay High Court in Income-tax Reference No. 51 of 1958.

A. V. Viswanatha Sastri, S. P. Mehta, J. B. Dodachanji, O.C. Mathur and Ravinder Narain, for the appellants. K. N. Rajagopal Sastri and R. N. Sachthey, for the respondent.

1962. December, 11. The judgment of the Court was delivered by-

HIDAYATULLAH, I.-This is an appeal on a certificate granted by the High Court of Bombay against the judgment and order of the High Court dated June 23, 1959. The appellants are two assesses whose cases were consolidated before the Tribunal and hence a single appeal. The facts of the case are as follows :

> Before the year 1938, the two appellants and one Jehangir Irani were carrying on business in electric goods including electric bulbs under two firm names. One of the firms was called the Precious Electric Co. and the other was named J. Pirojsha & Co. In June, 1938, Precious Electric Co. entered into an agreement with M/s. Philips Electrical Co. (India) Ltd. by which the Company demarcated a territory for the Firm, undertaking to sell and deliver electric bulbs therein exclusively to the Firm. By a letter which formed an annexure to the agreement the Company agreed to sell electric bulbs to the Firm at ex-warehouse prices subject to a commission of 12-21 %on the gross invoice amount and the Firm was allowed a further discount of 2% on the net invoice prices to cover breakage or fault in manufacture. It was further agreed that if the Company sold any goods directly to the buyers in the territory the Company would pay to the Firm compensation amounting to 5% of the net amount of invoices covering such sales. The Firm on its part undertook to sell only Philips bulbs in the territory and to prevent re-exportation of the bulbs by third parties. In addition to other conditions to which we need not refer at this stage there was a clause for termination of the agreement. The clause provided that the agreement would be deemed to have been made as from July 1, 1938, and would continue unless determined by either party by giving to the other party three months' prior notice by registered letter of such party's intention to determine the agreement on the June 30, 1939 or any subsequent June 30. This agreement continued for a period of sixteen years.

On March 8, 1954, the Company sent a letter to the Firm informing the Firm that the agreement would come to an end from June 30, 1954. The Company sent a draft of a new agreement which was intended to take the place of the earlier agreement. Some negotiations between the parties followed but no fresh agreement was signed . On May 28, 1954, the two assessees and the Manager of the Firm met the representatives of the Company to discuss the new agreement. Nothing much came of the discussion and since the Bombay branch of the Company was taking over the business of selling bulbs in the territory, a working scheme for the period immediately' following the termination of the existing agreement was reached. This was recorded in the shape of minutes which were signed by the represen. tatives of the Company and by the two partners of the Firm. The minutes covered arrangements for the period of transition, the stocks and the staff of the firm. Of these the important provisions are as follows :-

(a) PERIOD OF TRANSITION:

Philips Bombay Branch will continue the distribution of lamps, etc. to dealers and in this respect Messrs. Precious promised to furnish their name list of dealers and their supplies over the past six months. It was concluded that the execution of orders of locally available goods might be terminated in two months' time, whereas this matter as far as orders placed with overseas suppliers are concerned might take about five months.

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During this    period Messrs.  Precious will
receive all    co-operation from Messrs.  Philips
to ensure a    smooth winding up of the business.
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Furthermore, particular attention will be given to the I. S. D. contracts and transactions in connection with public bodies. Messrs. Precious will inform these bodies that the supplies will be effected through their intermediary by Philips Bombay, Branch which refers in particular to those cases where close personal contact between Messrs. Precious and the parties exists. The commission related to the above special cases,- executed after the termination of the existing agreement will be due to Messrs. Precious if no technical objection emanating from ELA'S agreement will come forward."

"'(b) STOCKS Messrs. Philips, Bombay will take care that the stocks of Messrs. Precious will be disposed of in one way or the other as soon as possible in order to avoid that Messrs. 'Precious' capital might unnecessarily be tied up. In order to achieve this, the available goods will be classified in three categories, viz

(i) Easily saleable goods.

(ii) Goods which require some sales efforts, which means that they might -be disposed of in a period of four to six weeks.

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(iii) Slow moving items which will be taken over by Bombay Branch.

The goods mentioned under (iii) above will be taken over by Messrs. Philips at the original invoice price if not otherwise decided due to deterioration of the goods whilst a deduction is valid for cost incurred for transfer." The following minutes, headed "Miscellaneous", were at the end and read :-

> "MISCELLANEOUS:As a gesture of goodwill, Messrs. Philips are prepared to pay in quarterly instalments to each of the three partners' during a period of three years, Rs. 40,000/- per annum from the date of the expiry of the existing contract. The three partners referred to above as far as Messrs. Philips Electrical Co., understand are Mr. Pirojsha H. Devecha

2. Mr. Khurshedji A. Irani

3. Mr. Noshir J. Irani Finally, Mr. Van Rhijn stated that Messrs. Philips are quite willing to continue Messrs. Precious as regular lamp dealers and the profit they realise therfrom will be in addition to the three years' remuneration referred to above."

In the account year ended December 31, 1954 relative to the assessment year 1955-56, each of the three partners received two quarterly payments of Rs. 10,000 each. This amount was taxed by the Income-tax Officer in respect of the two appellants as compensation under s. 10 (5A) of the income-tax Act. An assessment was also made on the third partner but we are not concerned with that assessment. The appellate Assistant Commissioner to whom the assessee appealed held that provisions of s. 10 (5A) did not apply to the facts of the case on the ground that the appellants were not agents of the Company from which payment had been received and the amount received was not compensation as no legal damage had been caused to them by the Company. He, however, held that the sum of Rs. 20,000 in respect of each of the appellants was a taxable receipt. The -assessees appealed to the Tribunal and four contentions were raised by them. They were "(i) it was compensation paid for termination of agreement which constituted the frame work of the Firm's business.

(ii) the amount was an ex-gratia payment made by way of testimonial.

(iii) the payment is made to individual partners and not to the firm as such and does not represent a receipt in the course of firm's business.

(iv) alternatively, the said receipt was not liable to be included in the total income of the recipient by reasons of Section 4 (3) (vii)."

The Tribunal did not accept these contentions but at the request of the firm referred three questions for the decision of the High Court. Those questions were as follows :-

whether the receipt of Rs. 20,000/- is a taxable receipt for the purpose of the Indian Income-tax Act, 1922 ?

(ii) If so, is it liable to be not included in the total income of the recipient by reason of Section 4 (3) (vii) ?

(iii) Does the said receipt fall within the mischief of Section 10 (5A) (d) and as such liable to tax accordingly ?"

The reference was heard by the High Court and the learned judges answered the -first question as follows :- "The receipt of Rs. 20,000/- is a taxable receipt for the purpose of the Indian Income-tax Act, 1922."

In view of the answer the High Court observed as follows :-

"As we have already held that the amount is taxable receipt, being receipt arising from business, Section 4 (3) (vii) does not exempt it from liability to tax. We are in the view we have taken not called upon to consider whether even if the receipt of Rs. 20,000/- is a capital receipt, by operation of Section 10 (5A) (d) the amount can be regarded as a revenue receipt. We answer the second question as follows :

It is liable to be included in the total income notwithstanding Section 4 because it arose from business."

The third question was left unanswered. The High Court certified the case as fit for appeal and hence this appeal. The High Court in reaching its conclusion examined the agreement of 1938 and come to the conclusion that though it involved a ""monopoly purchase" and gave to the Firm an exclusive right to sell Philips bulbs in the assigned territory, it was no more than a trading agreement which did not constitute a trading asset. By the loss of this monopoly right, the High Court went on to say, the business of the firm was not destroyed because even after the termination of the agreement the firm was entitled to carry on the business of selling electric bulbs as a ,-,regular lamp dealer". According to the High Court the agreement while it lasted only conferred on the Firm the right to obtain Philips bulbs on favourable terms as their stock-in-trade. By the termination of the agreement this right to acquire the stock-in-trade on favourable terms was lost but there was no capital loss as the business of selling bulbs continued. The High Court also referred to the minutes where the payment of Rs. 40,000 per annum to each of the partners for a period of three years was "expressly designated" 'three years remuneration'. They referred to numerous cases in which distinction has been made in India and in England between capital and revenue receipts. The learned judges ,distinguished those in which receipts were described as on the capital side. In particular they relied on the case in Bush, Beach & Gent. Ltd. v. Road (1). They distinguished between those cases in which the cancellation of the contract affected the structure of the assessee's business and those in which it did not, and held that this was a case in which the structure of the business of the Firm was not affected and the payment made must be treated as on the revenue side particularly because it was described as remuneration and was payable yearly for a period of three years. In the appeal before us Mr. Vishwanath Sastri has put the case of the appellants from two angles. He contends that the agreement was not a trading agreement but constituted an asset on the termination of which compensation was paid to make up for the loss of this capital asset. He contends that the (1) (1939) 22 Tax Cases 519.

agreement, though it could be terminated on the June 30 in any year with three months' notice, had run for sixteen years to the advantage of both the Company and the Firm and thus was always likely to run unless terminated. He points out that it involved a monopoly right to sell Philips bulbs exclusively in the territory assigned and also conferred other rights like favourable terms of purchase of bulbs, compensation for invasion of territory and a right to discount in case of breakage or faulty manufacture. In other words, the agreement was not an ordinary trading agreement by which the stock-in-trade was secured but involved something more than the purchase of stock-in-trade. It constituted the means of earning profits or as it is commonly described ,,,the money-making apparatus" of the appellants. When this agreement was terminated, he continued, it was not a premature termination but the expectancy was that it was to run unless terminated and the compensation which was paid though described as remuneration was, in a business sense, merely compensation for the loss of those rights which the Firm had enjoyed and which it expected to enjoy in the future if the agreement was not terminated.

In the alternative, Mr. Vishwanatha Sastri contends that even if the amount could not be referable to a loss of a capital asset it was not referable to any future service to be rendered by the assessees who had by the termination of the agreement become ordinary dealers in bulbs like any other dealer in the same territory. Nor was it referable to any past service but was a payment ex-gratia out of appreciation of the personal qualities of the partners whose services in the past were fully remunerated. In other words, this was an ad hoc payment in the nature of a 'testi- monial' as it is sometimes described or as a "solatium', by which term the Privy Council described the payment in Income-tax Commissioner v. Shaw Wallace & Co. (1) - (1) (1932) L.R. 59 I.A. 206.

Mr. K. N. Rajagopal Sastri on behalf of the Commissioner of Income-tax contends that the business of selling bulbs was only a part of the business activities of Precious Electric Co. and that Firm was one of the two firms carrying on the same or similar businesses. The agreement conferred the benefit of a favourable mode of acquiring stock-in-trade only and its termination did not lead to any loss of capital because it was not a capital asset in the hands of the Firm but was only a trading agreement, entered into in the ordinary course of business. Mr. Raiagopal Sastri contends that the monoply involved in the agreement was merely incidental to such a trading agreement and was not an asset which could be said to have been lost on the termination of the agreement. He contends that there was no premature termination as the agreement had worked itself out and even if treated as capital it had exhausted itself. An amount paid after capital has exhausted itself must be treated as revenue from 'other sources' within s. 12 of the Income-tax Act. He contends that even if the entire business activities of the assessees were confined to implementing the agreement it cannot be considered as capital because it had a very minor place in the entire business of the two firms which continued unaffected by the termination of the agreement. In reply to the argument that this was a "testimonial' or `solatium' Mr. Rajagopal Sastri contends that the minutes did not describe it as such but on the other hand stated that the payment was made to supplement the business receipt of the partners in the next three years. He accordingly contends that the judgment under appeal is right and this payment cannot be regarded either as a capital receipt or as an exgratia payment. Before we consider these questions and refer to the authorities which were cited at the bar we shall refer in some detail to the terms of the agreement of 1938 to find out its true nature so as to be able to decide whether it can be regarded as a trading agreement entered into for the purpose of obtaining the stock-in-trade for the business or it can be regarded as an asset. The agreement consisted of 13 clauses but all of them were not equally important. The first clause provided for two matters : (a) it fixed a territory and (b) it defined the scope of the agreement. In the first part were mentioned the Bombay Presidency, Rajputana, Central Provinces and Berar, and in the second part "all lamps for electrical lighting purposes"'of certain kinds (compendiously called 'Philips lamps') were said to be covered by -the agreement. Clause 2 was also divided into two parts. The first part said that the Company undertook to sell and/or to deliver Philips lamps exclusively to the Firm in the territory, the second part provided that should any buyer refuse to pur- chase from the Firm, the Company would make the supply direct but '.pay five per cent. compensation over the net amount of invoice covered in such orders ,to the Firm. Clause 3 recited the terms accepted by the Firm. This clause was also divided into two parts. The first part bound territory only such Philips lamps it by the Company.

prevent re-export of the lamps the Firm to sell in the as were supplied to The second part bound it to by third parties as far as possible. By clause 4 the Firm bound itself to observe clause 3 in respect of such lamps as might remain undisposed of with the Firm after the termination of the agreement. Clause 5 reserved to the Company the right to alter the prices rate of discount and conditions of sale without notice to the Firm even in respect of unexecuted contracts. Clause 6 reserved to the Company the right to refuse orders and/or to cancel or to suspend deliveries for any reason, whatever, including the reason that the prices obtaining had become unprofitable. That clause also provided that in case of such cancellation, cessation- or suspension of deliveries the Firm would not be entitled to receive -compensation. By clause 7 the Firm bound itself to push the sale of the Philips lamps according to the directions of the Company and not to sell lamps other than Philips lamps and not to support any firm competing with the Company in any way and to keep secret methods of work etc. Clause 8 then provided that the Firm would buy and sell Philip lamps on its own account and at its own risk. The rest of the terms need not be referred to. The gist of the agreement, therefore, was that the Firm was to have an exclusive territory for sale of Philips lamps and undertook to sell only Philips lamps in that territory. The agreement allowed the Finn compensation if Philips lamps were sold in the territory by the Company. There was no provision in the agreement how many lamps the Firm was to buy from the Company in a particular period and there was no condition that the Firm -would be required to buy any specified quantity and/or quality. There was no agreement that the Firm was to act as the agent of the Company. This was an agreement between principal and principal, the measure of the business depending upon how far the Firm wag able to push the sales of Philips lamps in its own interest and in the interest of the Company. The agreement was to commence on July 1, 1938, and was termi. nable by a three months notice on either side on June 30, of any year. It is fair to inforce that as long as the Company and the Firm found the arrangement profitable the agreement would have continued. By an annexure to the agreement, which was in the form of a letter, the terms of business between the Firm and the Company were laid down. This letter stated the commission payable to the Firm and the manner in which payments were to be made by the Firm. Sufficient reference to these terms has already been made by us in an earlier part of this judgment. This annexure was to be read as a part of the agreement. It was probably kept separate so that in case of need only the annexure might be altered without the trouble of executing a fresh agreement.

In determining whether this payment amounts to a return for loss of a capital asset or is income, profits or gains liable to income-tax, one must have regard to the nature and quality of the payment. If the payment was not received to compensate for a loss of profits of business the receipt in the hands of the appellant cannot properly be described as income, profits or gains as commonly understood. To consti- tute income, profits or gains, there must be a source from which the particular receipt has arisen, and a connection must exist between the quality of the receipt and the source. If the payment is by another person it must be found out why that payment has been made. It is not the motive of the person who pays that is relevant. More relevance attaches to the nature of the receipt in the hands of the person who receives it though in trying to find' out the quality of the receipt one may have to examine the motive out of which the payment was made. It may also be stated as a general rule that the fact that the amount involved was large or that it was periodic in character have no decisive bearing upon the matter. A payment may even be described as 'pay', 'remuneration' etc. but that does not determine its quality, though the name by which it has been called may be relevant in determining its true nature, because this gives an indication of how the person who paid the money and the person who received it viewed it in the first instance. The periodicity of the payment does not make the payment a recurring income because periodicity may be the result of convenience and not necessarily the result of the establishment of a source expected to be productive over a certain period. These general principles have been settled firmly by this Court in a large number of ,cases. See for example : The Commissioner of Income-tax v. Vazir Sultan, & Sons (1), Oodrej & Co, v. Commissioner of Income- tax (2), Commissioner of Income-tax v. Jairam Valji (3), Senairam Doongarmall v. Commissioner of Income-tax (4). (1) [1959] Sapp. 2 S.C.R. 375. (2) 11960] 1 S.C.R. 527. (3) [1959] 35 I.T.R. 148. (4) (1961] 42 I.T.R, 392.

We shall begin by considering whether the payment made in this case can be related to the termination of the agreement of 1938 and can be said to arise from that termination in the shape of compensation in lieu of profits. The agreement of 1938 did not state that on the termination of the agreement in the way provided there compensation was payable to the Firm. For temporary suspension of supplies no compensation was payable. These terms of the agreement show that though the agreement was to run its course as long as it proved profitable to the parties, at least the Firm was not entitled to be compensated either for a temporary suspension of the benefits under the agreement or a complete termination of those benefits. The payment cannot, there- fore, on the terms of the agreement be connected with loss of estimated profits. It was said, a long time ago in the well-known case of Glenboig Union Fireclay Co. Ltd. v. Commissioner of Inland Revenue (1) that there is no relation between the measure that is used for the purpose of calculating a particular result and the quality of the figure that is arrived at by means of application of that test. Here, the amount is large but there is nothing to show that it was ever) an adequate measure of the profits that were expected to be made during the three years in which the amount was to be paid. Even if it had been there would have been no inference in law. But in the absence of any proof that this was the likely profit it is difficult to say that the payment replaced those profits.

Another way of looking at the matter is to consider whether the agreement was a trading agreementor something which was in the nature of an asset in the hands of the firm. In this connection the Department relies strongly upon the case of Bush Beach & Gent. Ltd. v. Road (2). In that case ,the agreement was different. No doubt by that agreement also a territory was reserved (1) (1922) Tax Cas 427. (2) (1939) 2 Tax Cases 519.

and a monopoly was created but that agreement was to last for four years and was prematurely terminated at the end of two years. Under that agreement a minimum quantity of chemicals had to be bought and if the buyers failed to exercise their option to take up the minimum quantity in any one year, the contract itself was to be considered as terminated without any further option. The assessees in that case were industrial chemists till 1933 and by the agreement had offered to buy agricultural chemicals and had set-up, is a result of the agreement, a special organisation for selling agricultural chemicals. The amount of compensation on the premature termination of the agreement was arrived at after negotiations and the sum represented profits of the lost business and not the price for the purchase of the contract. It was observed by Lawrence, J., that the business of the assessee continued unaffected and that if a trading contract made in the ordinary course of business, though covering a new field, was prematurely

-terminated and compensation was paid for that premature termination, it must be considered to be in replacement of profits and not capital. In reaching this conclusion the learned judge pointed out that the case resembled Short Bros. Ltd. v. Commissioners of Inland Revenue (1) and Commissioner of Inland Revenue v. Northfleet Coal and Ballast Co. Ltd. () but was distinguishable from Ven den Berghts' case (3). In Short Brother's case (1) a trading contract was terminated and compensation was paid towards loss of profits in respect of that contract. Lord Hanworth M. R. observed that the payment was not compensation for not carrying on of the business but was a sum paid in the ordinary course in order to adjust the relation between the shipyard and its customers. In the same case Lawrence, L. J. observed that the payment was in the nature of an ordinary trading receipt on the termination of a trading agreement which might or might not have been profitable but on the termination of which the (1) (1927) 12 Tax Cas. 955. (2) (1927) 12 Tax Cas. 1102 (3) (1935) 19 Tax Cas. 390.

payment was made on the expectation that it would have been profitable. In Northfleet's case (1) compensation was paid to get rid of a contract under which supplies of chalk from a quarry had to be made. The purchaser received a payment of pound 900 a year and in return released the supplier from liability under the contract. Later a lumpsum of E. 3000 was accepted and this amount was held to be a trading profit. It was observed by Rowlatt, J.

> "'These contracts are not being sold. They are not being even extinguished really for this purpose. What is happening is that the profits under them are being taken ; something is being taken in respect of the profits of them. That is the position. This sum represents the profits of the Company on the contracts, treating them as contracts which notionally have earned or are going to earn a profit. Those profits are relating to this sum. The profits are not destroyed. It is the profits which we are concerned with, not the contract itself"

On the other side there is the leading case of Ven den Berghs Ltd. v. Clark (2) where mutual trading agreements between two companies were rescin. ded and one of the companies was paid lb. 450,000 as "'damages". This was treated as a capital receipt and not an income receipt to be included in computing the profits of the trade under Schedule D, Case 1, of the Income-tax Act 1918. Lord Macmillan described the payments as follows "On the contrary the cancelled agreements related to the whole structures of the appellants' profit-making apparatus. They, resulted the Appellants' activities, defined what they might and what they might not do, and affected the whole conduct of their business. I have difficulty in seeing how money laid out to secure, (1) (1927) 12 Tax Cas. I 10?.

(2) (1935) 19 Tax Cas. 390.

or money received for the cancellation of, so fundamental an Organisation of a trader's activities can be regarded as an income disbursement or an income receipt." The agreement in our case was not an agreement for the purchase of bulbs or lamps. It mentioned no quantity or quality or price. It only secured to the firm a right to exclusive purchase for sale in an exclusive territory. In other words, it created a monopoly right of purchase for and a monoploy right of sale in a certain territory. The agreement secured to the firm an advantage of an enduring nature. No doubt, the agreement was terminable in anyyear on three months' notice but it would have lastedas long as it was profitable to the contracting parties and the indications were that it was to subsist for some time. It was an agreement which need not have continued but which was likely to continue. The question, therefore, is whether by termination of the agreement the firm lost an advantage or merely lost the right to obtain certain stockin-trade for which they had bargained. If it was first then the receipt, if connected with that loss, was a capital receipt and if the latter it was a replacement of the profits which were likely to ensue from the trading agreement. In our opinion, it is impossi- ble to describe this agreement as a trading agreement. It can only be described as an agreement which constituted a source and a monopoly, and which gave an enduring advantage to a trader in his trade. The loss of such an agreement must be regarded as falling on the capital asset of the person affected and not in the course of his ordinary trading. If the agreement had been breached prematurely the damages would not have been calculated on the basis of outstanding contracts only but on the basis of an advantage lost. Indeed, the agreement itself contemplated in some of its terms other contracts under which the supplies were to be made and refers in terms to the cancellation of "'orders" and "contracts This shows that in addition to this agreement there were to be trading contracts in the shape of orders for bulbs which the Firm would have placed with the Company in the ordinary course of their business. The agreement said that even on the termination of those contracts and orders no compensation was payable. It is difficult to see how this payment can be related to profits or how it can be called income, profits or gains or even income from "'other sources." The payments can be regarded only as ad hoc pay- ments.

Even if it be not regarded as a payment for loss of capital it cannot be regarded as payment for any services rendered or likely to be rendered. The services in the past were amply remunerated. The payment does not contemplate that the agreement in the past had not been sufficiently remunerative to the Firm. It does not pretend to pay them for past services. The minutes do not show that any service in the future was expected from these appellants. What remained to be done was to wind up the business with regard to the agreement of 1938 itself. For this purpose, the Company agreed to give all facilities to the Firm in respect of easily saleable articles and to take over those which required a longer duration to sell. The only service, if service it can be called, was that the Firm was to hand over to the Company a list of customers and the supplies made to them during the past six months. It cannot be said that for this service the payment was made. The payment was thus not related to any service either in the past or in the future. Both sides have relied upon cases in which certain payments were held to be taxable or not taxable according as the facts in those cases suggested that the payment was for some services in the past or future or was entirely gratuitous. No useful purpose will be served by going over such cases because the facts of 969- two very dissimilar cases lead to different principles. We do not, therefore, refer to the cases of professional cricketers for whom benefit matches are held or who receive payments for outstanding performance with the bat or ball or cases of persons working in honorary capacity or in little- paid jobs who on retirement receive some payment in token of their worth. Those cases stand on their own facts. The safest method is to take the facts of the case in hand and to consider for what was the payment received and incidentally for what was the payment made. judged from this angle it is quite clear that the payment here was not made for any service. In fact it was not made to the firm but to the three partners individually. It was not related to any service that was likely to be performed in the future even though it -A as described as remuneration additional to the ordinary profits of trading. It was in no sense a remuneration. It was in fact a payment made out of regard for the qualities of the three partners of the firm who were'long associated with -the Company to its profit and who had built up a vast network of sales Organisation of which the Company would have obtained benefit when it entered on the business of selling for itself. This payment need not be given a particular name. It need not be called a 'testimonial' as to which Rowlatt, J, said in Chibbett v. Joseph Robinson & Sons (1) that there is no magic in that name. It need not be called a "solatium', a term devised by Rowlatt J, in the same case and applied by the Privy Council in Shaw Wallace's case (2) but which this Court did not adopt in Senairam Doongarmall's case (3) without attempting to give it a name we are satisfied that the payment was in token of appreciation and was not related to any business done or to loss of profits and it was not recompense for services past or future. It was a payment out of gratitude and must be regarded as a payment which does not bear the character of income, profits or gains which alone are taxable under the Income-tax Act. In our, opinion, the (1) [l924) 9 T.C. 49. (2) (1932) L.R. 59 I.A. 206 (3) [1959) 35 148 High Court, with all due respect, was in error in holding that this amount was taxable. The answer to the first question must therefore be against the Department. The next question is whether the receipt can be described under s. 4 (3) (vii) as of a casual and nonrecurring nature and not by way of addition to the remuneration of an employee. The assessees were not "employees" of the Company and were not in receipt of remuneration. After the termination of the agreement they were to work as regular leap dealers if they cared. Therewas,nocompulsion that they must sell electric lamps whether made by the Company or by other manufacturers. If they did, they were to receive commission at any other regular dealer. It is thus obvious that the latter part of s. 4 (3) (vii) does not apply. The receipt may only be described as a receipt of a casual and non-recurring nature if it were income, profits or gains. We have already said that the fact that payment was spaced over three years did not make this a recurring receipt. In our judgment the receipt would be saved by s. 4 (3) (vii) from being included in the total income in any event. But we are of opinion that not being income, profits or gains s. 4 (3) (vii) has no application. Our answer to the second question is that s. 4 (3) (vii) does not apply. The third question need hardly detain us. it was not answered by the High Court. 'Section 10 (5A) of the Act deals with four categories of persons. The first three categories ex- facie do not apply. The fourth category also does not apply as the appellants in their individual capacity were not holding "an agency" and the Firm -of which they were partners was also not an agent of the Company. The answer to that question must be against the Department. In view of what we have said above this appeal must succeed. It is allowed with costs on the respondent in this Court and in the High Court.

Appeal allowed.