HC-KAR

IN THE HIGH COURT OF KARNATAKA AT BENGALURU

DATED THIS THE 2ND DAY OF JUNE, 2025

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BEFORE

THE HON'BLE MR JUSTICE S.R.KRISHNA KUMAR

WRIT PETITION NO. 20212 OF 2023 (T-IT)

BETWEEN:

MANJEET SINGH CHAWLA
SON OF MR. JAWAHAR SINGH CHAWLA,
AGED ABOUT 40 YEARS,
RESIDING ATA-1/163, 16TH FLOOR,
DLF WESTEND HEIGHTS,
AKSHAYA NAGAR,
BENGALURU-560 068.

…PETITIONER

(BY SRI. TARUN GULATI, SENIOR COUNSEL FOR
SRI. PRADEEP NAYAK, & SRI. KISHORE KUNAL
MISS. ANKITA PRAKASH & SRI. SANKEETH VITTAL, ADVOCATES)

AND:

1. DEPUTY COMMISSIONER OF TDS
WARD-(1)(2), BANGALORE
HMT BUILDING
BENGLAURU – 560 095.

2. COMMISSIONER OF INCOME TAX
TDS, RANGE-1, BENGALURU
CENTRAL REVENUE BUILDING,
QUEENS ROAD,
BENGALURU-560 001.

…RESPONDENTS

(BY SRI. E.I. SANMATHI & SRI.M.DILIP, ADVOCATES)

THIS W.P IS FILED UNDER ARTICLE 226 OF THE CONSTITUTION OF INDIA, 1950 PRAYING TOA) QUASHING THE IMPUGNED ORDER DATED 02/08/2023 BEARING DIN. SO/20052023/476399 (ANNEXURE-A) PASSED BY THE R1 & ETC.,

THIS PETITION IS BEING HEARD AND RESERVED ON 15.01.2025 COMING ON FOR PRONOUNCEMENT OF ORDERS THIS DAY, THE COURT MADE THE FOLLOWING:-

CORAM: HON'BLE MR JUSTICE S.R.KRISHNA KUMAR

CAV ORDER

This petition takes an exception to the impugned order dated 02.08.2023 passed by the 1st respondent, whereby the request of the petitioner for issuance of 'Nil Tax Deduction Certificate' for Income Tax in favour of the petitioner for the financial year 2023-24 was rejected and for consequential directions to the respondents to issue the said 'Nil Tax Deduction Certificate' for Income Tax under Section 197 of the Income Tax Act, 1961 (for short 'the I.T. Act') and for other reliefs.

2. Briefly stated the facts giving rise to the present petition are as under:

Petitioner is an Indian Citizen and a salaried employee of Flipkart Internet Private Limited (FIPL) which is an Indian Subsidiary of Flipkart Marketplace Private Limited (FMPL), a Company incorporated in Singapore which is further a wholly owned subsidiary of Flipkart Private Limited, Singapore (FPS). In addition to FMPL, FPS has many other subsidiaries including

PhonePe which had a wholly owned subsidiary in India known as PhonePe India Private Limited.

2.1 In the year 2012, FPS introduced the Flipkart Stock Action Plan, 2012 (FSOP), pursuant to which the petitioner was granted 2232 stock options with a vesting schedule of four years from 01.01.2016 to 31.03.2023 amongst which 955 stock options were vested, 249 were cancelled and the unvested stock options were 1028, resulting in the total number of stock options held by the petitioner being 1983 as on 31.03.2023. Meanwhile, on 23.12.2022, FPS announced separation/divestment of PhonePe resulting in reduction and diminishing of the value of the stock options issued in favour of the petitioner. Under these circumstances, FPS announced a one time compensatory payment of USD 43.67 per option as compensation towards loss in value of FSOPs due to divestment/separation of PhonePe from FPS. In pursuance of the same, a sum of Rs.71,01,004/- i.e., 1983 x 43.67 x 82 (USD Conversion rate) was paid to the petitioner towards the aforesaid one time compensatory payment due to reduction/diminishing of the value of the stock options issued in favour of the petitioner as stated supra.

2.2 The petitioner filed an application dated 29.04.2023 under Section 197 of the I.T. Act seeking 'Nil Tax Deduction Certificate' in relation to the aforesaid one time compensatory payment made to him. Since there were certain errors in the said application, petitioner withdrew the said application dated 29.04.2023 and filed a fresh/modified application dated 20.05.2023 under Section 197 of the I.T Act. The respondents raised certain queries which were clarified by the petitioner vide reply/response dated 24.07.2023, pursuant to which, the 1st respondent proceeded to pass the impugned order rejecting the application filed by the petitioner, who is before this Court by way of the present petition.

3. Heard learned Senior Counsel for the petitioner and learned counsel for the respondents and perused the material on record.

4. In addition to reiterating the various contentions urged in the petition and referring to the material on record, learned Senior Counsel for the petitioner submitted that the 1st respondent committed an error in coming to the conclusion that the compensation of Rs.71,01,004/- received by him for reduction/diminution of the value of FSOPs was taxable as a

perquisite under the head 'Income from Salary' and that the profit or gain on sale/transfer of stocks exercised under FSOPs is liable to be taxed under the head 'Income from Capital Gains'. In this context, it is submitted that the compensation received from the petitioner does not fall under the definition "Income" and the same was a capital receipt which did not contain any element of income and hence, not chargeable to tax. It was also submitted that the consideration to be received by the petitioner would not amount to perquisites and consequently ,would not qualify as "Salary" so as to attract Section 17(2) (vi) of the I.T Act, since the compensation was in the nature of a capital receipt received by the petitioner for diminution/reduction of the value of the FSOPs. It is therefore submitted that the impugned order deserves to be quashed and the application filed by the petitioner under Section 197 of the I.T Act deserves to be allowed by issuing appropriate directions to the respondents to issue a 'Nil Tax Deduction Certificate' in favour of the petitioner at the earliest. In support of his submissions, learned Senior counsel placed reliance upon the judgment of the Delhi High Court in relation to compensation paid to one more identically situated employee of FIPL in respect of diminution/reduction of

value of FSOPs issued by FPS in the case of ***Sanjay Baweja Vs. Deputy Commissioner of Income Tax – (2024) 163 taxmann.com 116 (Delhi),*** wherein an identical/similar impugned order was quashed and the petition was allowed in favour of the said employee. He would also place reliance upon the following judgments:

(i) Padmaraje R. Kadambande vs. CIT - [1992] 195 ITR 877 (SC);

(ii) CIT v. Shaw Wallace & Co. - AIR 1932 PC 138;

(iii) Vijay Ship Breaking Corporation vs. CIT - [2009] 314 ITR 309 (SC);

(iv) CIT v/s. Canara Bank - [2016] 386 ITR 229;

(v) Commissioner of Wealth-tax vs. Ellis Bridge Gymkhana - [1997] 95 Taxmann 143 (SC);

(vi) Kettlewell Bullen & Co.Ltd. vs. CIT - [1964] 53 ITR 261 (SC);

(vii) M/s. Karam Chand Thapar & Bros. Pvt. Ltd. v/s. CIT (Central), Calcutta - (1972) 4 SCC 124;

(viii) Oberoi Hotel (P) Ltd. vs. CIT - [1999] 103 Taxmann 236 (SC);

(ix) Godrej & Co., Bombay vs. CIT, Bombay - (1960) 1 SCR 527;

(x) Senairam Doongarmall vs. CIT - [1961] 42 ITR (SC);

(xi) Commissioner of Income Tax, Gujarath vs. Saurashtra Cement Ltd., - [2010] 325 ITR 422 (SC);

(xii) CIT vs. B C Srinivas Shetty - [1981]128 ITR 294 (SC);

(xiii) CIT vs. D.P. Sandu Bros. Chembur (P.) Ltd., - [2005] 142 Taxmann 713 (SC)

(xiv) Cadell Wvg. Mill Co. (P) Ltd. v/s. CIT - [2011] 166 Taxmann 77 (Bombay);

(xv) Mathuram Agrawal v/s. State of Madhya Pradesh - (1999) 8 SCC 667;

(xvi) C Nanda Kumar vs. UOI - 396 ITR 21;

(xvii) Correspondent, Holy Cross Primary School v/s. CBDT - 388 ITR 162 (Mad);

(xviii) GE India Technology Centre Private Limited V/s. CIT - (2010) 10 SCC 2;

(xix) Sidhartha Sen vs. DCIT, TDS Chandigarh and Ors. – SWP 16336/2023;

(xx) Income Tax Officer v/s. Atchaiah - (1996) 1 SCC 417;

(xxi) Commissioner of Income Tax vs. Ajax Products Ltd., - (1965) 1 SCR 700;

(xxii) Bharat Financial Incusion Ltd. vs. DCIT, TDS, - (2018) 96 taxmann.com 540 (Hyd-Trib);

(xxiii) Empire Jute Co. Ltd. vs. CIT - [1980] 3 Taxmann 69 (SC);

(xxiv) PCIT v/s. Chemplast Sanmar Ltd., - [2022] 142 taxmann.com 515 (Mad.);

(xxvi) Manpowergroup Service India (P.) Ltd. v/s. CIT (TDS), New Delhi, - [2021] 123 taxmann.com 290 (Delhi);

(xxvii) Tata Teleservices (Maharashtra) Ltd. v/s. DCIT, TDS - [2018] 90 taxmann.com 1 (Bombay).

5. Per contra, learned counsel for the respondents-Revenue would reiterate the various contentions urged in the statement of objections and support the impugned order and submit that there is no merit in the petition and that the same is liable to be dismissed. It was submitted that the compensation to be received by the petitioner was not in the nature of a capital receipt and was a taxable revenue receipt. It was further submitted that receipt of any FSOP or any FSOP related to monetary benefit by the petitioner inherently carries the character of income and is taxable as perquisites and the compensation granted to the petitioner is the lost FSOPs and tax treatment of this compensation should be identical to the tax treatment of the FSOPs themselves. It was also submitted that the payment received by the petitioner is part of the perquisites value due to the petitioner and taxable under Section 17(2) of the I.T Act which is deemed/implied allotment of shares as per Section 17(2) of the I.T Act and the allotted stocks are sweat equity shares under Section 17(2)(vi)(b) of the I.T Act and the compensation to be received by the petitioner is part of the fair

market value that the petitioner is entitled to after the vesting period when he exercises the option. It was therefore submitted that in the light of the availability of the alternative remedy of revision under Section 264 of the I.T Act, the present petition was not maintainable and that the same is liable to be dismissed. In support of their submissions, learned counsel places reliance upon the judgment of the Madras High Court in the case of ***Nishithkumar Mukeshkumar Mehta Vs. Deputy Commissioner of Income Tax – W.P.No.26506/2023 and connected matters*** dated ***31.07.2024.***

6. I have given my anxious consideration to the rival contentions and perused the material on record.

7. In my considered opinion, the impugned order passed by the 1st respondent rejecting the application filed by the petitioner under Section 197 of the I.T Act for issuance of 'Nil Tax Deduction Certificate' is illegal, arbitrary and contrary to law and facts and the same deserves to be quashed and necessary direction are to be issued to the respondents to issue the said certificate in favour of the petitioner at the earliest for the following reasons:

(i) It is well settled that TDS cannot be deducted if payment does not constitute income and the power of the respondents-revenue to direct deduction of tax under Section 197 of the I.T. Act can be exercised only if there is an income chargeable to tax. In ***Padmaraje's*** case supra, the Apex Court held as under:

> *"21. We will now proceed to consider the correctness of these submissions. Section 2(24) of the Income Tax Act, 1961 defines in an inclusive manner what "income" is. The word "income" connotes periodical monetary return coming in with some regularity or expected regularity from definite sources. In E.D. Sassoon & Company Ltd. [(1954) 26 ITR 27, 49 : AIR 1954 SC 470 : (1955) 1 SCR 313] at page 49 this Court cited the Privy Council ruling in CIT v. Shaw Wallace & Co. [ILR (1932) 59 Cal 1343, 1350 : AIR 1932 PC 138 : 59 IA 206] wherein it was observed:*
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> *"Income, their Lordships think, in the Indian Income Tax Act, connotes a periodical monetary return coming in with some sort of regularity, or expected regularity from definite sources. The source is not necessarily one which is expected to be continuously productive, but it must be one whose object is the production of a definite return, excluding anything in the nature of a mere windfall."*
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> *32. This was the reason why we said neither the nomenclature nor the periodicity of the payment would be the determinative factors. Regard must be had only to the nature and quality of payment. The High Court took the view that this is not compensation. One thing that is certain is that the assessee lost her right to these allowances. Thereafter, on an application by way of compassion the*

payment is made. The mere fact, after the order is made it becomes an enforceable right, is neither here nor there. The reliance on Rameshwara Rao case [(1963) 49 ITR 144 : AIR 1967 SC 290 : (1964) 2 SCR 847] does not seem to be correct in view of what we have pointed out above.

33. It has already been seen that the marginal heading of Section 15 is "compensation". The fact that under clauses (i), (ii) and (iii) of Section 15(1) the compensation is paid as of right and in cases falling under clause (d) of the proviso, it is a discretionary payment, would not stamp the payment with a character of revenue. As to how a marginal heading has to be construed can be gathered from Chandroji Rao case [(1970) 2 SCC 23 : (1970) 77 ITR 743] . It is stated therein that the marginal heading to a section cannot control the interpretation of the words of the section particularly where the meaning of the section is clear and unambiguous.

34. For a moment, we are not interpreting the words of the section but we are only holding that even a payment under clause (d) is nothing but compensation because as the facts disclose the amount of Rs 10 lakhs out of a trust property in the Bank of Kolhapur was misappropriated.

35. There is no compulsion on the part of the Government to make the payment nor is the Government obliged to make the payment since it is purely discretionary. A case similar to the one on hand is H.H. Maharani Shri Vijaykuverba Saheb of Morvi [(1963) 49 ITR 594 (Bom)] head-note of which is extracted:

"A voluntary payment which is made entirely without consideration and is not traceable to any source which a practical man may regard as a real source of his income but depends entirely on the whim of the donor cannot fall in the category of income.

The ruler of a native State abdicated in favour of his son in January, 1948. From April, 1949, onwards his son paid him a monthly allowance. The allowance was not paid under any custom or usage. The allowance could not be regarded as maintenance allowance, as the assessee possessed a large fortune.

Held, that as the payments were commenced long after the ruler had abdicated, they were not made under a legal or contractual obligation. As the allowances were not also made under a custom or usage or as a maintenance allowance, they were not assessable."

36. The position is exactly the same. The payment made by the Government is undoubtedly voluntary. However, it has no origin in what might be called the real source of income. No doubt Section 15(1) proviso clause (d) enables the applicant to seek payment but that is far from saying that it is a source. Therefore, it cannot afford any foundation for such a source. Further, it is a compassionate payment, for such length of period as the Government may, in its discretion, order.

37. Lastly, we may refer to Kamal Behari Lal Singha case [(1971) 3 SCC 540 : (1971) 82 ITR 460] which is pressed into service by the Revenue, to support its contention one has to look at the character of the payment in the hands of the receiver and the source from which the

payment is made has no bearing on the question. We will extract the head-note (from ITR) of this ruling:

"During the accounting period ending April 13, 1950, the assessee, who was a shareholder in a company, received a dividend of Rs 13,200 from the company. Out of that amount a sum of Rs 8,829 was paid out of capital gains received by the company in the shape of salamis and land acquisition compensation receipts after March 31, 1948. The question was whether that part of the dividend attributable to salamis and compensation for land acquisition was taxable in the hands of the assessee:

Held, that the assessee had a beneficial interest in that sum in the hands of the company. Undoubtedly, the amount received by the company towards salami and compensation of acquisition of its lands was a capital receipt in the hands of the company and when the sum was distributed amongst its shareholders each of the shareholders took a share of the capital asset to which they were beneficially entitled. The receipt of Rs 8,829 was a capital receipt in the hands of the assessee. The fact that the sum was distributed as 'dividend' did not change the true nature of the receipt; a receipt was what it was and not what it was called.

Trustees of the Will of H.K. Brodie v. IRC [(1933) 17 Tax Cases 432 (KB)] applied

Held also, that that part of the dividend received by the assessee attributable to land acquisition compensation received by the company after March 31, 1948, was not

receipt of 'dividend' within the meaning of Section 2(6-A) of the Income Tax Act, 1922.

CIT v. Nalin Behari Lall Singha [(1969) 2 SCC 310 : (1969) 74 ITR 849] , followed

It is now well settled that in order to find out whether a receipt is a capital receipt or a revenue receipt one has to see what it is in the hands of the receiver and not its nature in the hands of the payer. In other words, the nature of the receipt is determined entirely by its character in the hands of the receiver and the source from which the payment is made has no bearing on the question. Where an amount is paid which, so far as the payer is concerned, is paid wholly or partly out or capital, and the receiver receives it as income on his part, the entire receipt is taxable in the hands of the receiver."

38. This is a case of compensation paid under the Land Acquisition Act. It was held that a compensation as such would be capital receipt in the hands of the receiver and the fact that it was distributed as dividends would not change the true nature of the receipt.

39. As a result of the above discussion, we hold that the amounts received by the assessee during the financial years in question have to be regarded as capital receipts and, therefore, are not income within the meaning of Section 2(24) of the Income Tax Act. Accordingly, we set aside the judgment of the High Court and allow the appeals with no order as to costs."

Similarly, in ***Shaw Wallace's*** case supra, the Privy Council held as under:

> *"The matter for consideration in the appeal was, in substance, whether the respondents, who carried on business as merchants and agents in Calcutta and elsewhere in India, were chargeable to income-tax under the above Act in respect of compensation paid to them for the termination of agencies for two oil-producing companies.*
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> *The facts of the case and the three questions referred appear from the judgment of the Judicial Committee.*
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> *The High Court, by a judgment delivered by Rankin C.J. and concurred in by C.C. Ghose and Buckland JJ., answered the first question in the affirmative, thereby holding that the sum of Rs.9,83,361/- (being the compensation received less admitted deductions) was a capital receipt and therefore did not come within the computation of the profits of the respondents' business. Having regard to that conclusion no answer was returned to the second and third questions. The Court was however of opinion, upon the authority of In re Turner Morrison & Co., that the receipt arose out of the business; also, that the exemption in s. 4, sub-s. 3 (vii), of the Act did not apply to the case. The proceedings are reported at I.L.R. 58 C. 1053.*
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> *1932. Feb. 5, 9, 11. Dunne K.C. and R.P. Hills for the appellant. The compensation (less the admitted deductions) is chargeable to tax under s. 6 (iv) of the*

Indian Income-tax Act, 1922, under the head "business." The agencies in respect of which the compensation was paid were part only of the respondents' business, and their business as merchants and agents continued after the payment; the compensation was a profit of the business in the year of account. There was no transfer of goodwill or any other dealing with the capital assets. As both the Commissioner and the High Court found that the compensation arose out of the business, it was chargeable to tax unless the assessees showed that it came within the exemptions in s. 10 or that it was a capital receipt not chargeable to tax. The Indian Act does not make the clear distinction between capital and income which there is under the English statutes; that is shown by s. 4, sub-s. 3 (v). The judgment of the High Court is not consistent with its judgment in Turner Morrison & Co. It was based upon Glenboig Union FireclayCo. v. Commissioner of Inland Revenue and Chibbett v. Joseph Robinson & Sons, both of which are distinguishable. The former was decided upon the ground that there had been a sterilization of a capital asset. In the latter case the assessees had rights under the articles of association and received a capital sum to release them. The decision was merely that there was evidence to support the finding of the Commissioner, whereas in the present case the Commissioner held that the receipt was not of a capital nature; the observations of Rowlatt J., relied on, were obiter. That the compensation received in this case was chargeable to tax is supported

by Hancock v. General Reversionary and Investment Co.; Commissioners of Inland Revenue v. Newcastle Breweries; Short Brothers v. Commissioners of Inland Revenue; Commissioners of Inland Revenue v. Gloucester Railway Carriage and Wagon Co.; Ensign Shipping Co. v. Commissioners of Inland Revenue; Burmah Shipping Co. v. Commissioners of Inland Revenue; J. Gliksten & Son v. Green. In Anglo-Persian Oil Co. v. Dale it was held that compensation paid by the then appellant company in the same circumstances as in this case was a revenue payment and therefore deductible in arriving at their net profits.

Latter K. C. and Cyril King for the respondents. The observations of Rowlatt J. in Chibbett's case, referred to in the judgment of the Chief Justice, were correct and are directly in point. The business there continued after the payment, as it did in this case. The money received was compensation for loss of part of the business as distinct from earnings of the business. Income is something which flows from the property or trade as distinct from something received in place of the property or trade, in whole or in part: Commissioners of Inland Revenue v. Blott and Pool v. Guardian Investment Trust Co., referring to Eisner v. Macomber. The idea of income flowing from a source is embodied in the Indian Act in sections. 4 and 12. The series of English cases referred to for the appellant are distinguishable upon their facts; they were mostly cases of contracts not going through. The decision in the Anglo-Persian Oil Co. case cannot be

applied to this case; the effect of an exemption or proviso cannot be used to extend the scope of a statutory provision: Commissioners for Special Purposes v. Pemsel; West Derby Union v. Metropolitan Life Assurance Society. The case In re Turner Morrison & Co. does not apply to the first question, because it was admitted that the receipt there in question was income; the contest there was whether it was exempt under s. 4, sub-s. 3 (vii). It is submitted that the judgment in that case was incorrect in distinguishing between "arising from business" and "profits of business."

Dunne K. C. in reply. The appellant relies upon the reasoning of the concluding part of the judgment last mentioned. Further, if the compensation was not income it was a "gain" within the meaning of s. 6 of the Act.

March 14. The judgment of their Lordships was delivered by Sir George Lowndes. This is an appeal from a judgment of the High Court at Calcutta delivered on a reference made to it under s. 66 of the Indian Income-tax Act XI. of 1922. The reference arose out of an assessment to income-tax upon the respondents for the year 1929—30, in respect of an item of Rs. 9,83,361, part of a larger sum of Rs. 15,25,000 received by them in 1928 as compensation for the termination of certain agencies.

The respondents carry on business in Calcutta as merchants and agents of various companies, and have branch offices in different parts of India. For a number of years prior to 1928 they acted as distributing agents in

India of the Burma Oil Company and the Anglo-Persian Oil Company, but had no formal agreement with either company. In or about the year 1927 the two companies combined and decided to make other arrangements for the distribution of their products. The respondents' agency of the Burma company was accordingly terminated on December 31, 1927, and that of the Anglo-Persian company on June 30 following. Some time in the early part of 1928 the Burma company paid to the respondents a sum of Rs. 12,00,000 "as full compensation for cessation of the agency," and in August of the same year the Anglo-Persian company paid them another sum of Rs.3,25,000/- as "compensation for the loss of your office as agents to the company." The quotations are from letters by which the payments were recorded, and are accepted on both sides as correctly expressing the nature of the transactions.

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

The respondents objected to the assessment, and appealed to the Assistant Commissioner, who confirmed the assessment. Thereafter, on the requisition of the

respondents, the Commissioner drew up a statement of the case, and referred the questions of law therein set out to the High Court with his own opinion thereon, which was against the contentions of the respondents.

The questions so formulated were as follows:—

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

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

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

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

The learned judges appear to have returned a formal answer only to question (a), which the Chief Justice stated to be "the real question in the case." He thought that if the

respondents could not escape by reason of the contention raised by this question they must fail. The other questions, he thought, fell within a recent decision of the Court in the case of In re Turner Morrison & Co; he had nothing to add to what was then said on these points.

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

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

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

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

The object of the Indian Act is to tax "income," a term which it does not define. It is expanded, no doubt, into "income profits and gains, "but is expansion is more a matter of words than of substance. Income, their Lordships think, in this Act connotes a periodical monetary return "coming in" with some sort of regularity, or expected regularity, from definite sources. The source is not necessarily one which is expected to be continuously

productive, but it must be one whose object is the production of a definite return, excluding anything in the nature of a mere windfall. Thus income has been likened pictorially to the fruit of a tree, or the crop of a field. It is essentially the produce of something which is often loosely spoken of as "capital." But capital, though possibly the source in the case of income from securities, is in most cases hardly more than an element in the process of production.

The sources from which the taxable income under the Act are to be derived are enumerated in s. 6, which runs as follows: "Save as otherwise provided by this Act, the following heads of income, profits and gains, shall be chargeable to income-tax in the manner hereinafter appearing, namely:—(i) Salaries. (ii) Interest on securities. (iii) Property. (iv) Business. (v) Professional earnings. (vi) Other sources."

The claim of the taxing authorities is that the sum in question is chargeable under head (iv) business. By s. 2, sub-s. 4, business "includes any trade, commerce or manufacture, or any adventure or concern in the nature of trade, commerce or manufacture." The words used are no doubt wide, but underlying each of them is the fundamental idea of the continuous exercise of an activity. Under s. 10 the tax is to be payable by an assessee under the head business "in respect of the profits or gains of any business carried on by him." Again, their Lordships think, the same central idea: the words italicized are an essential constituent of that which is to produce the taxable income:

it is to be the profit earned by a process of production. And this is borne out by the provision for allowances which follows. They include rent paid for the premises where the business is carried on; the cost of current repairs in respect of such premises; interest on money borrowed for carrying on the business, etc.

Some reliance has been placed in argument upon s. 4, sub-s. 3 (v), which appears to suggest that the word "income" in this Act may have a wider significance than would ordinarily be attributed to it. The sub-section says that the Act "shall not apply to the following classes of income," and in the category that follows, clause (v) runs: "Any capital sum received in commutation of the whole or a portion of a pension, or in the nature of consolidated compensation for death or injuries, or in payment of any insurance policy, or as the accumulated balance at the credit of a subscriber to any such provident fund."

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

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

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

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

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

For the reasons given their Lordships are of opinion that question (a) was rightly answered by the High Court in favour of the assessee. No objection has been taken to

the form of the answer or to its sufficiency, and it would seem unnecessary therefore to deal with the other two questions. Their Lordships will only add that the reasoning of this judgment would apply equally if the appellant based his claim on head (vi) "other sources" and the corresponding provisions of s. 12.

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

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

In ***Vijay Ship Breaking Corporation's*** case supra, the Apex Court has held as under:

"11. For the aforestated reasons, Question 2 as to whether the assessee was bound to deduct TDS under Section 195(1) is answered in favour of the assessee and against the Department. The assessee was not bound to deduct tax at source once Explanation 2 to Section 10(15)(iv)(c) stood inserted as TDS arises only if the tax is assessable in India. Since tax was not assessable in India, there was no question of TDS being deducted by the assessee. Therefore, Question 2 is

answered in favour of the assessee and against the Department."

In ***Canara Bank's*** case supra, the Punjab and Haryana High Court held as under:

"8. The Commissioner of Income-tax (Appeals) and the Tribunal on appreciation of material on record have concurrently recorded that if an organisation is exempted from payment of tax there was no need for deduction of tax at source by the assessee. Learned counsel for the Revenue was not able to demonstrate that the approach of the Commissioner of Income-tax (Appeals) and the Tribunal was erroneous or perverse or that the findings of fact recorded were based on misreading or misappreciation of evidence on record. The view of the Commissioner of Income-tax (Appeals) and the Tribunal is in conformity with the decision of the apex court in Hindustan Coca Cola Beverage P. Ltd. v. CIT (2007) 293 ITR 226 (SC), where it has been held as under (page 230):

"Be that as it may, the Circular No. 275/201/95-IT(B), dated January 29, 1997, issued by the Central Board of Direct Taxes, in our considered opinion, should put an end to the controversy. The circular declares 'no demand visualized under section 201(1) of the Income-tax Act should be enforced after the tax deductor has satisfied the officer-in-charge of TDS, that taxes due have been paid by the deductee-assessee. However, this will not alter the liability to charge interest under section 201(1A) of the Act till the date of payment of taxes by the deductee-assessee or the liability for penalty under section 271C of the Income-tax Act'."

(ii) The material on record discloses that the subject compensation received by the petitioner does not constitute income and is not chargeable to tax and rather it is a capital receipt being one time voluntary compensation received by the petitioner which does not satisfy taxability in accordance with the charging section; the said subject one time voluntary compensatory payment is against the fall in value of stock options allotted to petitioner which is the profit making structure of the petitioner and therefore, the payment is of capital receipt in nature, which is not subject / exigible / amenable to tax. In this context, it is relevant to refer to the judgment of the Apex Court in ***Ellis Bridge Gymkhana's*** case supra, wherein it was held as under:

> *"5. The rule of construction of a charging section is that before taxing any person, it must be shown that he falls within the ambit of the charging section by clear words used in the section. No one can be taxed by implication. A charging section has to be construed strictly. If a person has not been brought within the ambit of the charging section by clear words, he cannot be taxed at all.*
>
> *31. This judgment really goes against the contention made on behalf of the Revenue. The Court first laid down that a charging section of a taxing statute has to be strictly construed. The Court found that the charging*

section of various taxing statutes had imposed tax on Hindu Undivided Families as well as on "individuals". It has been held under various fiscal statutes that Mapilla Tarwads cannot be taxed as a Hindu Undivided Family but will have to be taxed as an "individual". If "individual" is understood under the Wealth Tax Act, in the same sense in which it has been understood in various fiscal statutes, then "individual" under Section 3 of the Wealth Tax Act will include a Mapilla Tarwad. But in the various tax Acts mentioned in that judgment "individual" has not been interpreted to include a firm or an association of persons.

32. That the charging section of the Wealth Tax Act does not impose a charge on a firm or association of persons has been made clear by explanatory notes on the provisions relating to direct taxes issued by the Central Board of Direct Taxes on 29-6-1981 clarifying the Finance Bill, 1981. The idea behind introduction of the new Section 21-AA was explained in the following words:

"21.1 Under the Wealth Tax Act, 1957, individuals and Hindu Undivided Families are taxable entities but an association of persons is not charged to wealth tax on its net wealth. Where an individual or a Hindu Undivided Family is a member of an association of persons, the value of the interest of such member in the association of persons is determined in accordance with the provisions of the rules and is includible in the net wealth of the member.

21.2 Instances had come to the notice of the Government where certain assessees had resorted to the creation of a large number of associations of persons without specifically defining the shares of the members therein with a view to avoiding proper tax liability. Under the existing provisions, only the value of the interest of

the member in the association which is ascertainable is includible in his net wealth. Accordingly, to the extent the value of the interest of the member in the association cannot be ascertained or is unknown, no wealth tax is payable by such member in respect thereof.

21.3 In order to counter such attempts at tax avoidance through the medium of multiple associations of persons without defining the shares of the members, the Finance Act has inserted a new Section 21-AA in the Wealth Tax Act to provide for assessment in the case of associations of persons which do not define the shares of the members in the assets thereof. Sub-section (1) provides that where assets chargeable to wealth tax are held by an association of persons (other than a company or a cooperative society) and the individual shares of the members of the said association in income or the assets of the association on the date of its formation or at any time thereafter, are indeterminate or unknown, wealth tax will be levied upon and recovered from such association in the like manner and to the same extent as it is leviable upon and recoverable from an individual who is a citizen of India and is resident in India at the rates specified in Part I of Schedule I or at the rate of 3 per cent, whichever course is more beneficial to the Revenue."

33. It will appear from this notification that the Central Board of Direct Taxes clearly recognised that the charge of wealth tax was on individuals and Hindu Undivided Families and not on any other body of individuals or association of persons. Section 21-AA has been introduced to prevent evasion of tax. In a normal case, in assessment of an individual, his wealth from every source will be added up and computed in accordance with provisions of the Wealth Tax Act to arrive at the net wealth which has to be taxed. So, if an individual has any interest in a firm or any other non-corporate body, then his interest in those bodies or associations will be added up in his wealth. It is only where such addition is not

possible because the shares of the individual in a body holding property is unknown or indeterminate, resort will be taken to Section 21-AA and association of individuals will be taxed as association of persons."

In ***Kettlewell Bullen's*** case supra, the Apex Court held as under:

"The appellant is a public limited Company, and has its registered office at Calcutta. By an agreement dated May 1, 1925, Fort William Jute Company Ltd., appointed the appellant its managing agent upon certain terms and conditions set out therein. Under the agreement the appellant was to receive as managing agent remuneration at the rate of Rs 3000 per month, commission at the rate of ten per cent on the profits of the Company's working, additional commission at three per cent on the cost price of all new machinery and stores purchased by the managing agent outside India on account of the Company, and interest on all advances made by the managing agent to the Company on the security of the Company's stocks, raw materials and manufactured goods. The appellant and its successors in business, whether under the same or any other style or firm, unless they resigned their office were entitled to continue as managing agent until they ceased to hold shares in the capital of the Company of the aggregate nominal value of Rs 1,00,000 and were on that account removed by a special resolution of the Company passed at an Extraordinary meeting of the Company, or until the

managing agent's tenure was determined by the winding up of the Company. In the event of termination of agency in the contingencies specified the managing agent was to receive such reasonable compensation for deprivation of office, as may be agreed upon between the managing agent and the Company and in case of dispute, as may be determined by two arbitrators. By clause 8, the managing agent was at liberty at any time to resign the office of managing agent by leaving at the registered office of the Company previous notice in writing of its intention in that behalf. The agreement did not specify any period for which the managing agency was to enure. Since the successors of the appellant were also to continue as agents, unless they resigned or became disqualified, the duration was in a sense unlimited. But by virtue of Section 37-A(2) of the India Companies Act, 1913, the appointment of the appellant as managing agent would expiry on January 14, 1957 i.e. on the expiry of twenty years from the date on which the Indian Companies (Amendment) Act, 1956, was brought into operation. Section 87-A(2), however, did not prevent the managing agent from being reappointed after the expiry of that period.

2. Beside the managing agency of Fort William Jute Co. Ltd. the appellant held at all material time managing agencies of five other limited companies viz. Fort Gloster Jute Manufacturing Co. Ltd., Bowreach Cotton Mills Co. Ltd., Dunbar Mills Ltd., Mothola Co., Ltd., and Joonktollee Tea Co. Ltd. The appellant had advanced Rs 12,50,000

to Fort William Jute Co. Ltd. on the security of the stocks, raw materials and manufactured goods of that Company. The appellant held in 1952, 600 out of 14,000 ordinary shares of the face value of Rs 100 each, and 6920 out of 10,000 preference shares also of the face value of Rs 100 each. On May 21, 1952 the appellant entered into an agreement with M/s Mugneeram Bangur and Co., the principal conditions of which were:

(i) M/s Mugneeram Bangur and Co., to purchase the entire holding of shares of the appellant in Fort William Jute Co. Ltd. — ordinary shares at Rs 400 each and preference shares at Rs 185 each and to make an offer to all holders of the company's shares — preference and ordinary to purchase their holdings at the same rates:

(ii) M/s Mugneeram Bangur and Co, to procure repayment on or before June 30, 1952 of all loans made by the appellant to the principal Company:

(iii) Ms Mugneeram Bengur and Co., to procure that the principal Company will compensate the appellant for loss of office in the sum of Rs 3,50,000, such sum being payable to the appellant after it submitted its resignation as managing agent; and

(iv) M/s Mugneeram Bangur and Co., to reimburse the Company the amount payable to the appellant.

The reasons for which the appellant agreed to relinquish the managing agency were set out in a letter dated May 28, 1952, addressed by the appellant to the members of the Company intimating that M/s Mugneeram Bangur and Co., were willing to purchase the shares at the same

rates at which they had agreed to purchase the shareholding of the appellant. It was recited in the letter that the installation of modern machinery in the Company's factory entailed heavy capital expenditure and it was necessary to obtain a loan secured by debentures charged on the Company's property; that large sums were required for renewals and replacements of machinery and it was not possible to obtain additional bank accommodation; that the appellant had made large advances to the Company exceeding Rs 12,50,000 and, having regard to its other commitments, it was doubtful if it would be able to make available to the Company additional finance that the arrangement with M/s Mugneeram Bangur and Co., by acceptance of the terms offered by them, was the most satisfactory method of solving the Company's difficulties; that it was in the best interest of the shareholders to terminate the appointment of the appellant which in the normal course would not fall due for renewal until January 14, 1957; that M/s Mugneeram Bangur and Co., had agreed to procure that Fort William Jute Co., Ltd. will pay to the appellant Rs 3,50,000 and that M/s Mugneeram Bangur and Co., will reimburse the Company for the payment, it being anticipated that they will in due course be appointed managing agents of the Company.

3. The arrangement with M/s Mugneeram Bangur and Co. was carried out. The appellant tendered its resignation with effect from July 1, 1952, in pursuance of the terms of the agreement and M/s Mugneeram Bangur

and Co. were appointed as managing agent of the Company. The sum of Rs 3,50,000 received by the appellant from the Company — which it is common ground was provided by M/s Mugneeram Bangur and Co. — was credited in the profit and loss account of the appellant as received from Fort William Jute Co. Ltd. on account of compensation for loss of office. But in arriving at the net profit in the return for income tax for the year 1953-54 this amount was deleted. In the proceedings for assessment for the year 1953-54 the Income Tax Officer, Companies District IV, Calcutta, included this amount in the appellant's taxable income. In appeal the Appellate Assistant Commissioner modified the assessment holding that the sum of Rs 3,50,000 received by the appellant as compensation for surrendering the managing agency, which was to enure for five years more, and which in normal course might have continued for another term of twenty years, was a capital receipt. The Appellate Tribunal confirmed the order of the Appellate Assistant Commissioner, observing that compensation received under an agreement for "an outright sale of such an agency to a third party", not being one which a businessman enters in the normal course of business, nor being one which amounts to modification, alteration or discharge of normal incidents of such a business, was not assessable to income tax as a revenue receipt.

4. At the instance of the Commissioner of Income Tax, the Tribunal referred under Section 66(1) of the Income

Tax Act, 1922, the following question to the High Court of Judicature at Calcutta:

"Whether on the facts and in the circumstances of the case the sum of Rs 3,50,000 received by the assessee to relinquish the managing agency was a revenue receipt assessable under the Indian Income Tax Act?"

The High Court, for reasons which we will presently set out, answered to the question in the affirmative. With certificate granted by the High Court, this appeal is preferred by the appellant.

5. This case raises once again the question whether compensation received by an agent for premature determination of the contract of agency is a capital or a revenue receipt. The question is not capable of solution by the application of any single test : its solution must depend on a correct appraisal in their true perspective of all the relevant facts. As observed in CIT v. Rai Bahadur Jairam Valji [35 ITR 148, 152] by Venkatarama Aiyar, J.

"The question whether a receipt is capital or income has frequently come up for determination before the courts. Various rules have been enunciated as furnishing a key to the solution of the question, but as often observed by the "highest authorities, it is not possible to lay down any single test as infallible or any single criterion as decisive in the determination of the question, which must ultimately depend on the facts of the particular case, and the authorities bearing on the question are valuable only as indicating the matters that have to be taken into account in reaching a decision.

Vide, Van Den Berghs Ltd. v. Clark [(1935) 3 ITR (Engl Cas) 17] . That, however, is not to say that the question is one of fact, for, as observed in Davies (H.M. Inspector of Taxes) v. Shell Company of China Ltd. [(1952) 22 ITR (Suppl) 1] 'these questions between capital and income, trading profit or no trading profit, are questions which though they may depend no doubt to a very great extent on the particular facts of each case, do involve a conclusion of law to be drawn from those facts'."

The interrelation of facts which have a bearing on the question propounded must therefore first be determined. The managing agency was not, except in the circumstances set out in clause 2 of the agreement, liable to be determined at the instance of the Company before January 14, 1957, unless the appellant by giving notice of three weeks voluntarily resigned the agency. At the date of termination the agency had five more years to run, and the Companies Act did not prohibit renewal of the agency in favour of the appellant, after the expiry of the initial period of twenty years. The appellant Company was formed for the object, amongst others, [vide clause 3(2) of the memorandum of association of the appellant] of carrying on the business of managing agencies. The appellant was entitled under the terms of the agreement to receive so long as the agency enured ten per cent of the profits of the Company's working, three per cent on all purchases of stores and machinery abroad, and a monthly remuneration of Rs 3000. The appellant submitted its resignation in exercise of the power

reserved under clause 8 of the meaning agency agreement, but that resignation was it is common ground part of the arrangement with M/s Mugneeram Bangur and Co. dated May 21, 1952. Under the terms of the managing agency agreement, the principal Company was not obliged to pay any compensation to the appellant for voluntary resignation of the agency, but in consideration of the appellant parting with its shareholding and submitting resignation of the managing agency so as to facilitate the appointment of M/s Mugneeram Bangur and Co. as managing agent, the latter purchased the shareholding of the appellant, undertook to make available Rs 3,50,000 for payment to the appellant and to discharge the debt due by the Company to the appellant. Payment of Rs 3,50,000 as therefore an integral part of an arrangement for transfer of managing agency. A managing agency of Company is in the nature of a capital asset; that is not denied. It is true that it is not like an ordinary asset capable of being transferred from one person to another. Theoretically, the power to appoint or dismiss the managing agent may lie with the directors of the Company, but in practice the power lies with the person or persons having a controlling interest in the shareholding of the Company, M/s Mugneeram Bangur and Co. were anxious to be appointed managing agents of the principal Company; and for that purpose the appellant had to be persuaded to agree to a premature termination of its agency. This was secured for a triple consideration : sale of shares held by the appellant at an

agreed price, stipulation to discharge the liability of the Company to repay the loans due by the Company, and payment of Rs 3,50,000 as compensation for termination of the appellant's agency.

6. The High Court summarised the effect of the agreement between the appellant and M/s Mugneeram Bangur and Co., as follows : The sum of Rs 3,50,000 described as compensation of loss of office of the managing agent was part of the whole scheme incorporated in the agreement. Each clause of the agreement was a consideration of the other clauses and payment of compensation for the alleged loss of office did not, being part of the total scheme, stand by itself. Determination of the managing agency of the appellant was not compulsory cessation of business : it was a voluntary resignation for which under the agency agreement the appellant was not entitled to any compensation, but by the device of procuring a purchaser the appellant was doing "business of selling the managing agency and getting a profit and value for it which it otherwise could not have got". The High Court stamped this transaction with the nature and character of a trading or a business deal, because in their view the managing agency of a Company — a institution peculiar to Indian business conditions — which creates a managing agent as an alter ego of the managed Company with authority to utilise the existing structure of the Company's organisation to carry on business, earn profits, and in fact, virtually to trade in every possible

sphere open to the Company, may be regarded as circulating capital, where several managing agencies are conducted by an assessee. Therefore in the view of the High Court the compensation received for surrendering the agency was remuneration received on account of conducting the business, and was income. The judgment of the High Court proceeded substantially upon the following two grounds:

(1) that on the facts of the case, the managing agency held by the appellant of Fort William Jute Co., Ltd. was stock-in-trade; and

(2) that the appellant was formed with the object of acquiring managing agencies, and in fact held managing agencies of as many as six companies. Earning profits by conducting the management of companies, being the business of the appellant, compensation received as consideration for surrendering the managing agency was a revenue receipt.

7. We are unable to agree with the High Court that the managing agency of Fort William Jute Co. Ltd. was an asset of the character of stock-in-trade of the Company. The appellant was formed with the object, among others, of acquiring managing agencies of companies and to carry on the business and to take part in the management, supervision or control of the business or operations of any other Company, association, firm or person and to make profit out of it. That only authorised the appellant to acquire as a fixed asset, if a managing agency may be so described, and to exploit it for the

purpose of profit. But there is no evidence that the Company was formed for the purpose of acquiring and selling managing agencies and making profit by those transactions of sale and purchase. A managing agency is not an asset for which there is a market, for it depends upon the personal qualifications of the agent. Counsel appearing on behalf of the Commissioner conceded that the case that the managing agency was of the nature of stock-in-trade was not set up before the Tribunal, and he does not rely upon this part of the reasoning of the High Court in support of the plea that the compensation received by the appellant is a revenue receipt. He relies upon the alternative ground, and contends that the managing agency of Fort William Jute Co. Ltd. was a part of the framework of the business of earning profit by working as managing agent of different companies, and in the normal course, termination of employment by the pripcipal companies of the appellant as managing agent being a normal incident of such business compensation received by the appellant is not for loss of capital but must be regarded as a trading receipt, especially when the termination of the agency does not impair the structure of the business of the appellant.

8. In the present case there is a special circumstance which must first be noticed. In truth of the amount of Rs 3,50,000 was received by the appellant from M/s Mugneeram Bangur and Co., in consideration of the former agreeing to forego the agency which it held and which M/s Mugneeram Bangur and Co. were anxious to

obtain. It was in a business sense a sale of such rights as the appellant possessed in the agency to M/s Mugneeram Bangur and Co. This is supported by the recitals made in clause 2 of the agreement that if at any time within six months after the completion of such sale M/s Mugneeram Bangur and Co. were unable to exercise the voting rights attached to the shares purchased by them, the appellant will appoint any person nominated by M/s Mugneeram Bangur and Co. to attend and vote for them at any meeting of the Company or the holders any class of shares to be held within such period in such manner as M/s Mugneeram Bangur and Co., may decide. The object underlying the agreement was therefore to transfer the managing agency to M/s Mugneeram Bangur and Co. or at least to effectuate their appointment in place of the appellant as managing agent of Fort William Jute Co., Ltd. All the stipulations and the covenants of the agreement, viewed in the light of the surrounding circumstances, do stamp the transaction as one of surrender of the rights of the appellant in the managing agency so that corresponding rights may arise in favour of M/s Mugneeram Bangur and Co. It would be irrelevant in considering the true nature of the transaction, to project the somewhat legalistic consideration that a managing agency is not transferable. It is because it is not directly transferable, that the arrangement incorporated in the agreement was effected. It would be difficult to regard such a transaction relating to a managing agency as a trading transaction.

9. Counsel for the assessee contended that even assuming that the form of the transaction under which for loss of the managing agency the appellant received compensation from the principle Company is decisive, or has even a dominate impact, and the ultimate source from which the compensation was provided is to be ignored, the compensation received for loss of agency by the agent must always be regarded under the Indian Income Tax Act as capital receipt. In support of that contention counsel placed strong reliance upon the judgment of the Judicial Committee in CIT v. Shaw Wallace and Co. [LR 59 IA 206] . In the alternative counsel pleaded that even if the extreme proposition was not found acceptable, the right of the assessee in the managing agency of the principal Company was to ensure for another five years and which in the normal course would have continued for another twenty years was an enduring asset and consideration received by the appellant for extension of that asset was a capital receipt.

10. On behalf of the Income Tax Department it was contended that Shaw Wallace and Co. case [(1935) 3 ITR (Engl Cas) 17] does not lay down any proposition of general application to compensation paid for determination of all agency contracts. It was further submitted that, having regard to the nature of the agreement and the voluntary resignation submitted by the assessee, no enduring asset remained vested in the assessee, and none was attempted to be transferred : the compensation directly paid by the principal Company

(which compensation was under the terms of the contract not payable) was only a "measure of profit" which the appellant would, but for the resignation, have earned, and was therefore in the nature of revenue. It was also urged that compensation was not payable to the assessee when resignation of the managing agency was tendered under clause 8 of the agreement and therefore the amount sought to be brought to tax was received by the assessee in the course of a normal trading transaction of the assessee. Finally, it was urged that in any event, by the loss of the agency the framework of the business of the assessee was not at all impaired, and therefore also the compensation received must be regarded as revenue and not capital.

11. Whether a particular receipt is capital or income from business, has frequently engaged the attention of the courts. It may be broadly stated that what is received for loss of capital is a capital receipt : what is received as profit in trading transaction is taxable income. But the difficulty arises in ascertaining whether what is received in a given case is compensation for loss of a source of income, or profit in a trading transaction. Cases on the borderline give rise to vexing problems. The Act contains no real definition of income; indeed it is a term not capable of a definition in terms of a general formula. Section 2(6-C) catalogues broadly certain categories of receipts which are included in income. It need hardly be said that the form in which the transaction which gives rise to income is clothed and the name which is given to it

are irrelevant in assessing the eligibility of receipt arising from a transaction to tax. It is again not predicated that the income must necessarily have a recurrent quality. We are not called upon to enter upon an extensive area of enquiry as to what receipts may be regarded as income generally, but merely to consider in this case whether receipt of compensation for surrendering the managing agency may be regarded as capital or as revenue. In the absence of a statutory rule, payment made by an employer in consideration of the employee releasing him from his obligations under a service or agency agreement or a payment made voluntarily as compensation for determination of right to office arises not out of employment, but from cessation of employment and may not generally constitute income chargeable under Sections 10 and 12. It may be mentioned that this rule has been altered by the legislature by the enactment of Section 10(5-A) by the Finance Act of 1955, which provides that compensation or other payment due to or received by a managing agent of an Indian Company at or in connection with the termination or modification of his managing agency agreement with the Company, or by a manager of an Indian Company at or in connection with the termination of his office or modification of the terms and conditions relating thereto, or by any person managing the whole or substantially the whole affairs of any other Company in the taxable territories at or in connection with the termination of his office or the modification of the terms and conditions relating thereto,

or by any person holding an agency in the taxable territories for any part of the activities relating to the business of any other person, at or in connection with the termination of his agency or the modification of terms and conditions relating thereto, shall be deemed to be profits and gains of a business carried on by the managing agent, manager or other person, as the case may be, and shall be liable to tax accordingly. But this amendment was made under the Finance Act, 1955, with effect from April 1, 1955, and has no application to the present case.

12. The Indian Income Tax Act is not in pari materia with the English Income Tax Statutes. But the authorities under the English law which deal not with the interpretation of any specific provision, but on the concept of income, may not be regarded as proceeding upon any special principles peculiar to the English Acts so as to render them inapplicable in considering problems arising under the India Income Tax Act. It is well-settled in England that money paid to compensate for loss caused to an assessee's trade is normally regarded as income. In Short Bros. Ltd. v. Commissioner of Inland Revenue [12 TC 955] a sum received as compensation for loss resulting from cancellation of a contract was held to be revenue in the ordinary course of the assessee's trade, and liable to excess profits duty. Similarly in Commissioners of Inland Revenue v. Northfleet Coal and Ballast Co. Ltd. [12 TC 1162] , compensation paid by a person who had agreed to purchase a certain quantity of chalk yearly for ten years, from a Company which was

the owner of a quarry, in consideration of being relieved of his liability under the contract was held chargeable to excess profits duty as trading profit in the hands of the Company.

13. In Commissioners of Inland Revenue v. Newcastle Breweries Ltd. [12 TC 97] compensation received under an order of the War Compensation Court, under the Indemnity Act, 1920, in addition to what was paid by the Admiralty for rum taken over in exercise of the power under the Defence of the Realm Regulations was held to be revenue.

14. In Ensign Shipping Co. Ltd. v. Commissioners of Inland Revenue [1 TC 1169] an amount paid by the Government to a ship-owner to compensate him for loss resulting from detention of his ships during a coal-strike, and for wages etc. was held liable to excess profits duty. Again as held in Burmah Steam Ship Co. Ltd. v. Commissioners of Inland Revenue [16 TC 97] money received by a ship-owner from a firm of ship-builders to compensate for loss resulting from the failure by the latter to complete repairs to ship within the stipulated period was regarded as revenue.

15. These cases illustrate the principle that compensation for injury to trading operations, arising from breach of contract or in consequence of exercise of sovereign rights, is revenue. These cases must, however, be distinguished from another class of cases where compensation is paid as a solatium for loss of office. Such compensation may be regarded as capital or

revenue : it would be regarded as capital, if it is for loss of a asset of enduring value to the assessee, but not where payment is received in settlement of loss in a trading transaction.

16. In Chibbet v. Joseph Robinson and Sons [9 TC 48] the assessees who were ship-managers employed by a steamship Company under a contract which provided that they should be paid a percentage of the Company's income, were paid compensation for loss of office in anticipation of liquidation of the steamship Company. It was held that payment to make up for loss resulting from cessation of profits from employment was not itself an annual profit, but was payment in respect of termination of employment and was not assessable to tax.

17. In Du Cross v. Ryall [19 TC 444] the assessee settled a claim made by his employee for damages for wrongful dismissal and paid £57,250 as compensation for wrongful dismissal. It was held that no part could be apportioned to salary and commission and the whole escaped assessment.

18. In Duff v. Barlow [23 TC 633] the Managing Director of the appellant Company who was employed for a period of ten years was asked by it to manage the business of one of its subsidiaries, and to receive a percentage of profits made by the subsidiary. The employment was terminated by mutual agreement two years after its commencement and £4000 were paid as compensation to the Managing Director for loss of his rights of future remuneration. This was held not taxable,

because it was a sum paid as compensation for loss of a source of income and hence a capital asset. This case was followed in Honley v. Murray [31 TC 351] where the appellant employed as a Managing Director of a property Company under a service agreement which was not determinable till March 31, 1944, was also appointed a Director of a subsidiary Company. At the request of the Board of Directors of the property Company the appellant resigned his office in the property Company as well as its subsidiary and received from the property Company an amount equal to the remuneration which he would, under the agreement, have been entitled to if his appointment had not been determined. It was held by the Court of Appeal that the use of the expression "compensation for loss of office" was not the determining factor when the bargain itself stood cancelled, and the sum paid was in consideration of total abandonment of all contractual rights which the other party had. The receipt was in the circumstances not taxable. The payment was not voluntarily made the bargain was that the appellant should resign and in consideration thereof, the Company should make the payment.

19. In Barr, Crombie and Co. Ltd. v. Commissioners of Inland Revenue [26 TC 406] appellant Company managed the ships of another Company under an agreement for a period of fifteen years. The shipping Company went into liquidation and a sum exceeding £16,000 was paid to the appellant Company for the eight years which were still to run to the date of expiry of the

agreement. Over a period upwards of sixteen years only two per cent of the appellant Company's income was derived from other managements, and on the liquidation of the shipping Company the appellant Company lost its entire business except for some abnormal and temporary business. It was held by the Court of Session in Scotland that the sum in question was not a trading receipt of the appellant Company. Lord President Normand observed:

> *"In the present case virtually the whole assets of the appellant Company consisted in this agreement. When the agreement was surrendered or abandoned practically nothing remained of the Company's business. It was forced to reduce its staff and to transfer into other premises, and it really started a new trading life. Its trading existence as practised up to that time had ceased with the liquidation of the shipping Company."*

20. These cases establish the distinction between compensation for loss of a trading contract and solatium for loss of the source of income of the assessee.

21. But payment of compensation for loss of office is not always regarded as capital receipt. Where compensation is payable under the terms of the contract which is determined, payment is in the nature of revenue and therefore taxable. For instance in Henry v. Foster [(1931) 145 LTR 225] it was held that when compensation stipulated under a contract is paid for loss of office, it is taxable under Schedule 'E', and it was also held in Dale v. D.E. Soissons [(1950) 2 AIR 460] that compensation paid under an agreement to an assistant of the Managing Director for premature termination of employment was held to be income. The principle on which these cases proceeded was also applied by the

Court of Session in Scotland in Kelsall Parsons and Co. v. Commissioners of Inland Revenue [21 TC 608] to a case in which there was no express term for payment of compensation on termination of employment. The appellants in that case carried on business as agents on a commission basis for sale in Scotland of the products of various manufacturers, and entered into agency agreement for the purpose. At the instance of the manufacturer concerned one of the agreements which was for a period of three years were terminated at the end of the second year in consideration of a payment of £1500. It was held by the Court of Session that no capital asset of the assessee was depreciated in value, or became of less use for the purpose of the assessor's business. The sum paid was accordingly included in the calculation of the taxable profits for the year in which it was received. Lord President Normand observed at p. 620.

> *"We are not embarrassed here by the kind of difficulties which arise when, by agreement, a benefit extending over a tract of future years is renounced for a payment made once and for all. The sum paid in this case is really and substantially a surrogatum for one year's profits."*

The foundation of the distinction made in Kelsall Persons and Co [21 TC 608] : Henslty v. Foster [(1931) 145 LTR 225] and Dale v. De Soissonsery is to be found in the observations made by Lord Macmillan in Van Den Berghs Ltd. v. Clark [TC 390] . In that case two companies which were manufacturers of margarine and similar products entered into an agreement with a view to and competition

between them and to work in friendly alliance and to share the profits and losses in accordance with an elaborate scheme. This arrangement was terminated by mutual agreement in consideration of the payment by the Dutch Company £4,50,000 to the appellant Company as damages. It was held by the House of the Lords that amount was received by the appellant as payment for cancellation of the appellant Company's future rights under the agreements, which constituted a capital asset of the Company, and that it was a capital receipts. Lord Macmillan observed at p. 431.

> *"Now what were the appellants giving up? They gave up their whole rights under the agreements for thirteen years ahead. These agreements are called in the States case 'pooling agreements' but that is a very inadequate description of them, for they did much more than merely embody a system of pooling and sharing profits. If the appellants were merely receiving in one sum down the aggregate of profits which they would otherwise have received over a series of years, the lump sum might be regarded as of the same nature as the ingredients of which it was composed. But even if a payment is measured by annual receipts, it is not necessarily in itself an item of income."*

23. In Wiseburgh v. Domvile [26 TC 527] the appellant had entered into an agreement in 1942 under which he acted as sole agent for the manufacturer. In 1948 when this agreement could have been determined by notice expiring in October 1949, the manufacturer dismissed him. The appellant received 4000 as damages for breach of agreement. The appellant had several agencies from time to time as agents and it was one of the incidents of agency business that one agency may be stopped and

another may be stopped and another may come and it being normal incident of the kind of business that the appellant was doing, that an agency should come to an end, compensation paid was regarded as income on the principle laid down in Kelsall Persons and Co. case [21 TC 608] .

24. In another case which soon followed Anglo-French Exploration Co., Ltd. v. Claysons [36 TC 545] the appellant Company carried on business, among others, as secretary and agent for a number of other companies. A South African company appointed the appellant Company as its secretary and agent at remuneration of a £1500 per annum under a contract terminable at six months' notice. Under on arrangement with the purchaser of the controlling interest of the shareholders under which the appellant Company was to resign its office as secretary and agent of the South African company, an amount of £20,000 received by the appellant Company was held by the Court of Appeal in the nature of a trading receipt.

25. In Blackburn v. Close Bros Ltd. [9 TC 164] the respondent Company carried on business of merchant bankers and of a finance and issuing house and derived income in the form of allowances for performing managerial and secretarial services. Following a dispute with one 'S' for which the respondent Company had agreed to provide secretarial services for three years at a remuneration of £8000 per annum, the agreement was terminated with about 2½ months from the date of its

commencement. £15,000 received by the respondent Company as compensation for termination of the agreement was held to be a trading receipt. Pennycuick, J., held that the contract was one of a number of ordinary commercial contracts for rendering services by the assessee in the course of carrying on its trade, and therefore the sum received on the cancellation of the agreement was a receipt of a revenue nature.

26. It is manifest that the principle broadly stated in the earlier cases, that compensation for loss of office, or agency, must be regarded as a capital receipt, has not been approved in later cases. An exception has been engrafted upon that principle that where payment even if received for termination of an agency agreement, but the agency is one of many which the assessee holds, and the termination of the agency does not impair the profit making structure, but is within the framework of the assessee's business, it being a necessary incident of the business that existing agencies may be terminated and fresh agencies may be taken, the receipt is revenue and not capital.

27. A case on the other side of the line may be noticed : Sabine v. Lookers Ltd. [38 TC 120] Under agreements, annually renewed with the manufactures, the respondent Company had acted for many years as their main distributors in the Manchester area of the manufacturer's products, which it bought for resale. The respondent had sunk considerable sums in fixtures and equipment specially designed for the trade of wholesale

dealers and carried a large stock of spare parts mainly for wholesale sale. The whole of the trade of the respondent was geard to the display, sale, service and repairs of the manufacturer's products. Up to 1952 inclusive, the manufacturers had included in its agreements with distributors a standard "continuity clause" giving the distributors, on certain conditions, the option of renewal for a further year. But in 1953, the manufactures, adopted a new standard agreement, containing a new continuity clause which the respondent Company regarded as giving it less security than before. As compensation for loss resulting from the alterations, the manufacturers paid to the respondent Company, a sum calculated on sales to the trade during the contract period. It was held that this was a capital receipt, because by the modification the framework of the respondent's business was impaired.

28. Elaborate arguments were presented before us on the decision of the Judicial Committee in Shaw Wallace and Co. case [LR 59 IA 206] . The appellant contended that Shaw Wallace and Co. case [LR 59 IA 206] laid down a principle of general application applicable to all cases of compensation received from the principal as solatium for determination of the contract of agency. Counsel for the Revenue contended that the principle should be restricted to its special facts, and cannot be extended in view of the later decisions, it is necessary to closely examine the facts which gave rise to that case. Shaw Wallace and Company carried on business as merchants and agents of various companies and had

branch offices in different parts of India. For a number of years they acted as distributing agents in India for the Burma Oil Company and Anglo Persian Oil Company, but without a formal agreement with either Company. The two Oil Companies having combined decided to make other arrangements for distributing their products. Each company terminated its contract with Shaw Wallace and Company and paid compensation to it, which aggregated to Rs 15,25,000. This amount, subject to certain allowances was sought to be assessed to income tax under Sections 10 and 12. The High Court of Calcutta held that the compensation received by the assessee was a capital receipt. In appeal to his Majesty-in-Council the decision of the High Court was armed.

29. The Judicial Committee declined to seek inspiration from the English decisions cited at the Bar. The Board observed that the expression "income" which is not defined in the Act connotes a periodical monetary return coming in with some sort of regularity, or expected regularity, from definite sources : the source is not necessarily one which is expected to be continuously productive, but it must be one whose object is the production of a definite return, excluding anything in the nature of a mere windfall. They further observed that the income chargeable under head (iv) of Section 6 "business" read with Section 10 is to be in respect of the profits and gains of any business carried on by the assessee, and therefore the sums which the Income Tax Department sought to charge could only be taxable if they

were the produce or the result of carrying on the agencies of the oil companies in the year in which they were received by the assessee. But when once it was admitted that they were sums received, not for carrying on this business, but as some sort of solatium for its compulsory cessation, the answer seemed fairly plain. The Board observed that if compensation received for sale of the business or its goodwill was capital, the same reasoning ought to apply when the sum received was in the nature of a solatium for cessation of a part of the business, and it was a matter of no consequence that the assessee continued to pursue its other independent commercial interests, and profits from which were taxed in the ordinary course, for the sums sought to be taxed had no connection with the continuance of the assessee's other business : the profits earned by the assessee, it was observed, "were the fruit of a different tree, the crop of a different field", and if under Section 10 the compensation was not taxable, it was not taxable under Section 12 under the head "other sources" as well.

30. The judgment of the Board proceeds upon the ground that compensation received not for carrying on the business but as solatium for its compulsory cessation, would be regarded as capital receipt, and for the application of this principle, existence of other independent commercial interests out of which profits were earned by the assessee was irrelevant. Two comments may be made at this stage. It cannot be said as a general rule, that what is determinative of the nature

of the receipt is extinction or compulsory cessation of an agency or office. Nor can it be said that compensation received for extinction of an agency may always be equated with price received on sale of goodwill of a business. The test, applicable to contracts for termination of agencies is : what has the assessee parted with in lieu of money or money's worth received by him which is sought to be taxed? If compensation is paid for cancellation of a contract of agency, which does not affect the trading structure of the business of the recipient, or involve loss of an enduring asset, leaving the taxpayer free to carry on his trade released from the contract which is cancelled, the receipt will be a trading receipt : where the cancellation of a contract of agency impairs the trading structure, or involves loss of an enduring asset, the amount paid for compensating the loss is capital.

31. The view expressed by the Judicial Committee has not met with unqualified approval in later cases. Lord Wright in Raja Bahadur Kamakshya Narain Singh of Ramgarh v. CIT, Bihar and Orissa [LR 70 IA 180] observed that it is incorrect to limit the true character of income, by such picturesque similies like "fruit of a different tree, or crop of a different field". Again it cannot be said generally that compensation for every transfer or determination of a contract of agency is capital receipt : Kelsall Persons and Co. v. Commissioners of Inland Revenue [21 TC 608] ; Commissioners of Inland Revenue v. Fleming and Co. [33 TC 57]

; Wiseburgh v. Domvillt [26 TC 527] and Commissioner of Income Tax and Excess Profits Tax, Madras v. South India Pictures Ltd. [29 ITR 910] . Nor is it true to say that where an assessee holds several agency contracts each agency contract cannot without more be regarded an independent of the other contracts, and income received from each contract cannot always be regarded as unrelated to the rest of the business continued by the assessee. The decision in Shaw Wallace Co case [LR 59 IA 206] cannot therefore be read to yield the principle that compensation for loss of an agency may in all cases be regarded as capital receipt. Nor does it lay down that where the assessee has several lines of business line must in ascertaining the character of compensation for loss of a line of business be deemed an independent source. This view is examplied by decisions of this Court and decision of the Madras High Court. In the South India Pictures Ltd case [29 ITR 910] compensation received for determination of the distribution rights of films was held taxable. After the assessee had exploited partially its right of distribution of cinematographic films to which it was entitled under the terms of agreement under which he had advanced money to the producers, the agreements were cancelled and the producers paid an aggregate sum of Rs 26,000 to the assessee towards commission. It was held by Das, C.J., and Venkatarama Aiyer, J., (Bhagwati, J., dissenting) that the sum paid to the assessee was not compensation for not carrying on its business, but was a sum paid in the ordinary course of business to adjust the

relations between the assessee and the producers, and was taxable. Similarly in Rai Bhahdur Jairam Valji case [35 ITR 148, 152] a contract for the supply of limestone and dolomites was terminated when the purchaser Bengal Iron Company Ltd. found the rates uneconomical. A suit was then filed by the respondent for specific performance of the contract and for an injunction restraining the Company from purchasing limestone and dolomite from any other person. A fresh agreement made between the respondent and the Company fell through because of circumstances over which the parties to the agreement had no control. The Company then agreed to pay Rs 2,50,000 to the respondent as solatium, besides the monthly instalments of Rs 4000 remaining unpaid under the contract of 1940. The Income Tax Department sought to bring to tax the amount of Rs 2,50,000 and the balance due towards the monthly instalments of Rs 4000. It was held by this Court that the sum of Rs 2,50,000 was not paid to the respondent as compensation for expenses laid out for works at the quarry of a capital nature and could not be held to be a capital receipt on that account, the agreements were merely adjustments made in the ordinary course of business. There was in the view of the Court no profit-making apparatus set up by the agreement of 1941, apart from the business which was to be carried on under it and there was at no time any agreement which operated as a bar to the carrying of the business of the respondent and therefore the receipt of Rs 2,50,000 was chargeable to tax. Venkatarama Aiyar,

J., observed, in an agency contract the actual business consists of dealings between the principal and his customers, and the work of the agent is only to bring about the business : What he does is not the business itself, but something which is intimately and directly linked up with it. The agency may, therefore, be viewed as the apparatus which leads to the business rather than the business itself. Considered in this light the agency right can be held to be of the nature of a capital asset invested in business. But this cannot be said of a contract entered into in the ordinary course of business. Such a contract is part of the business itself, not something outside it, and any receipt on account of such a contract can only be a trading receipt. Because compensation paid on the cancellation of a trading contract differs in character from compensation paid for cancellation of an agency contract, it should not be understood that the latter is always, and as a matter of law, to be held to be a capital receipt. An "agency contract which has the character of a capital asset in the hands of one person may assume the character of a trading receipt (asset) in the hands of another, as for example, when the agent is found to make a trade of acquiring agencies and dealing with them". Therefore, when the question arises whether the payment of compensation for termination of an agency is a capital or a revenue receipt, it must be considered whether the agency was in the nature of a capital asset in the hands of the agent, or whether it was only part of his stock-in-trade. The learned Judge also observed that payments

made in settlement of rights under a trading contract are trading receipts and are assessable to revenue, but where a trader is prevented from doing so by external authority in exercise of a paramount power and is awarded compensation therefor, whether the receipt is a capital receipt or a revenue receipt will depend upon whether it is compensation for injury inflicted on a capital asset or on stock-in-trade.

32. In Peirce Laslie and Co. Ltd. v. CIT, Madras [38 ITR 356] the assessee Company took up managing agencies of several plantation companies. The managing agencies were liable to termination, but the assessee was entitled to compensation by the terms of the agreement. Talliar Estates Ltd. was one of the companies managed by the assessee. The agreement was a composite agreement about the managing agency rights and certain other rights. When Talliar Estates Ltd. went into liquidation the assessee received Rs 60,000 by way of compensation for loss of office and the question arose whether that amount was income in the hands of the assessee. The Madras High Court held that the loss of one of several managing agencies had little effect on the structure of the assessee's business even in tea or on its profit earning apparatus as a whole and the termination of the agreement with Talliar Estates could well be said to have been brought about in the ordinary course of business of the assessee and therefore the amount received was a trading receipt.

33. In the South India Pictures Ltd. case [29 ITR 910] : Rai Bahadur Jairam Valji case [35 ITR 148, 152] and Peirce Leslie Companies case [38 ITR 356] it was held that the receipt of compensation for loss of agency was in the nature of revenue. In the South India Pictures Ltd case [29 ITR 910] the amount received was not compensation for not carrying on its business, but was a sum paid in the ordinary course of business to adjust the relations between the assessee and the producers : the termination of the agreements did not radically or at all affect or alter the structure of the assessee's business, and the amount received by the assessee was only so received towards commission i.e. as compensation for the loss of commission which it would have earned, had the agreements not been terminated. Therefore, the amount was not received by the assessee as the price of any capital assets sold or surrendered or destroyed, but the amount was simply received by the assessee in the course of its going distributing agency business and therefore it was an income receipt. In that case the majority of the Court held on three distinct grounds viz. (i) that the assessee did not part with any capital asset; (ii) that the amount was received in the course of the distributing agency business which was continued; and (iii) that the termination of the agreements did not radically or at all affect or alter the structure of the assessee's business, that the sum received was revenue. Rai Bahadur Jairam Valji case [35 ITR 148, 152] was one of compensation received for termination of a

trading contract. In Peirce Leslie and Company case [38 ITR 356] there was termination of office, but it was held to be brought about in the ordinary course of the trading operations of the assessee.

34. On the other side of the line are cases of Commissioner of Income Tax Hyderabad-Deccan v. Vazir Sultan and Sons [36 ITR 175] and Godrej and Co. v. CIT, Bombay City [37 ITR 381] . In Vazir Sultan and Son's case [36 ITR 175] the majority of the Court held that compensation paid for restricting the area in which a previous agency agreement operated was a capital receipt, not assessable to income tax. It was held that the agency agreements were not entered into by the assessee in the carrying on of their business, but formed the capital asset of the assessee's business which was exploited by the assessee by entering into contracts with various customers and dealers in the respective territories : it formed part of the fixed capital of the assessee's business and was not circulating capital or stock-in-trade of their business and therefore payment made by the Company for determination of the contract or cancellation of the agreement was a capital receipt in the hands of the assessee.

35. In Godrej and Co. case [37 ITR 381] the managing agency agreement in favour of the assessee of a limited Company which was originally for a period of thirty years and under which the assessee was entitled to a commission at certain rates was modified and remuneration payable to the managing agents was

reduced. As compesation for agreeing to this reduction, the assessee received Rs 7,50,000 which was sought to be taxed as income in the hands of the assessee. This Court held, having regard to all the attending circumstances, that the amount was paid not to make up the difference between the higher remuneration and the reduced remuneration, but in truth as compensation for releasing the Company from the onerous terms as to remuneration as it was in terms expressed to be : so far as the assessee firm was concerned it was received as compensation for the deterioration or injury to the managing agency by reason of the release of its rights to get higher remuneration and, therefore, a capital receipt.

36. On an analysis of these cases which fall on two sides of the dividing line, a satisfactory measure of consistency in principle is disclosed. Where on a consideration of the circumstances, payment is made to compensate a person for cancellation of a contract which does not affect the trading structure of his business, nor deprive him of what in substance is his source of income, termination of the contract being a normal incident of the business, and such cancellation leaves him free to carry on his trade (freed from the contract terminated) the receipt is revenue : Where by the cancellation of an agency the trading structure of the assessee is impaired, or such cancellation results in loss of what may be regarded as the source of the assessee's income, the payment made to compensate for cancellation of the agency agreement is normally a capital receipt.

37. In the present case, on a review of all the circumstances, we have no doubt that what the assessee was paid was to compensate him for loss of a capital asset. It matters little whether the assessee did continue after the determination of its agency with Fort William Jute Co. Ltd. to conduct the remaining agencies. The transaction was not in the nature of a trading transaction, but was one in which the assessee parted with an asset of an enduring value. We are, therefore, unable to agree with the High Court that the amount received by the appellant was in the nature of revenue a receipt.

38. We accordingly record the answer on the question submitted by the Tribunal in the negative. The appellant would be entitled to its costs in this Court."

In ***Karan Chand Thapar's*** case supra, the Apex Court held as under:

"8. As held by this Court in CIT v. Chari & Chari Ltd. [AIR 1966 SC 54 : (1965) 3 SCR 692 : 57 ITR 400] that ordinarily compensation for loss of office or agency is regarded as a capital receipt, but this rule is subject to an exception that payment received even for termination of an agency agreement would be revenue and not capital in the case where the agency was one of many which the assessee held and its termination did not impair the-profit-making structure of the assessee but was within the framework of the business, it being a necessary incident of the business that existing agencies may be terminated and fresh

agencies may be taken. But it is for the income tax department to clearly establish that the case fell within the exception to the ordinary rule. In the present case according to the findings of the tribunal, the termination of the agency in question had resulted in the destruction of a source of income of the company. The tribunal had arrived at the conclusion that the managing agencies held by the company represented the sources from which it received its income by way of commission.

9. In the determination of the question whether a receipt is capital or income, it is not possible to lay down any single test as infallible or any single criterion as decisive. The question must ultimately depend on the facts of the particular case, and the authorities bearing on the question are valuable- only as indicating the matters that have to be taken into account in reaching a decision. That, however, is not to say that the question is one of fact, for these questions between capital and income trading profit or no trading profit, are questions which, though they may depend to a very great extent on the particular facts of each case, do involve a conclusion of law to be drawn from those facts — see CIT, v. Rai Bahadur Jairam Vaji [AIR 1959 SC 291: 35 ITR 148] ; P.V. Divecha (deceased) and after him his legal Representatives v. CIT. [AIR 1964 SC 758: 48 ITR 222] ; Kettlewell Bullen & Co. Ltd. v. CIT [AIR 1965 SC 65 : 53 ITR 261 : (1964) 8 SCR 93] ; Gillanders Arbuthnot and Co. Ltd. v. CIT,

Calcutta [AIR 1965 SC 452 : 53 ITR 283 : (1964) 8 SCR 121] and CIT, v. Best & Co. (P) Ltd. [AIR 1966 SC 1325 : 60 ITR 11]

10. The question whether a particular income arising from the termination of one of the agencies of a multi-agency concern is a capital receipt or a revenue receipt is undoubtedly a difficult question to be answered. The difficulty is inherent in the problem itself. Decisions on this question are numerous. But none of them have laid down a precise principle of universal application but various workable rules have been evolved for guidance. One of us speaking for the Court in Kettlewell Bullen Co. case has laid down the following guidelines for finding out the true nature of such a receipt. The relevant observations read thus:

> *"Where on a consideration of the circumstances, payment is made to compensate a person for cancellation of a contract which does not affect the trading structure of his business, nor deprive him of what in substance is his source of income, termination of the contract being a normal incident of the business, and such cancellation leaves him free to carry on his trade (freed from the contract terminated) the receipt is revenue; where by the cancellation of an agency the trading structure of the assessee is impaired, or such cancellation results in loss of what may be regarded as the source of the assessee's income, the payment made to compensate for cancellation of the agency agreement is normally a capital receipt.*

In ***Oberoi Hotel's*** case supra, the Apex Court held as under:

"4. On the basis of the said agreement, the assessee has received a sum of Rs 29,47,500 from the

Receiver after the sale of the Hotel. The question which was considered by the Income Tax Authorities was whether the receipt of the said amount is capital receipt or revenue receipt. The Income Tax Officer arrived at a conclusion that it was a revenue receipt, the Commissioner of Income Tax (Appeals) held that it was a capital receipt, the Tribunal confirmed the said finding, on reference to the High Court, the High Court arrived at a conclusion that it was a revenue receipt assessable to income tax as business income for Assessment Year 1979-80. Hence, this appeal by special leave by the assessee.

5. The question whether the receipt is capital or revenue is to be determined by drawing the conclusion of law ultimately from the facts of the particular case and it is not possible to lay down any single test as infallible or any single criterion as decisive. This Court in the case of Karam Chand Thapar & Bros. (P) Ltd. v. CIT [(1972) 4 SCC 124 : 1973 SCC (Tax) 614 : (1971) 80 ITR 167] discussed and held that in CIT v. Chari and Chari Ltd. [(1965) 57 ITR 400 : AIR 1966 SC 54] it was held that ordinarily compensation for loss of an office or agency is regarded as capital receipt, but this rule is subject to an exception that payment received even for termination of an agency agreement would be revenue and not capital in the case where the agency was one of many which the assessee held and its termination did not impair the profit-making structure of the assessee, but was within

the framework of the business, it being a necessary incident of the business that existing agencies may be terminated and fresh agencies may be taken. Thereafter the Court held that it was difficult to lay down a precise principle of universal application but various workable rules have been evolved for guidance.

6. Applying the aforesaid test laid down by this Court in the present case, in our view the Tribunal was right in arriving at a conclusion that it was a capital receipt. The reason is that as provided in Article XVIII of the first agreement, the assessee was having an option or right or lien, if the owner desired to transfer the Hotel or lease a part of the Hotel to any other person, the same was required to be offered first to the assessee (Operator) or its nominee. This right to exercise its option was given up by a supplementary agreement which was executed in September 1975 between the Receiver and the assessee. It was agreed that the Receiver would be at liberty to sell or otherwise dispose of the said property at such price and on such terms as he may deem fit and was not under any obligation requiring the purchaser thereof to enter into any agreement with the Operator (assessee) for the purpose of operating and managing the Hotel or otherwise and in its return, the agreed consideration was as stated above in clause 10. On the basis of the said agreement, the assessee has received the amount in question. The amount was received because the assessee had given up its right to purchase and/or to

operate the property. Further it is a loss of source of income to the assessee and that right is determined for consideration. Obviously therefore, it is a capital receipt and not a revenue receipt.

11. The aforesaid principle is relied upon in the case of Karam Chand Thapar and Bros. [(1972) 4 SCC 124 : 1973 SCC (Tax) 614 : (1971) 80 ITR 167] Considering the aforesaid principles laid down as per Article XVIII of the principal agreement, the amount received by the assessee is for the consideration for giving up his right to purchase and or to operate the property or for getting it on lease before it is transferred or let out to other persons. It is not for settlement of rights under trading contract, but the injury is inflicted on the capital asset of the assessee and giving up the contractual right on the basis of the principal agreement has resulted in loss of source of the assessee's income."

In ***Godrej's*** case supra, the Apex Court held as under:

"8. This sum of Rs.7,50,000/- has undoubtedly not been paid as compensation for the termination or cancellation of an ordinary business contract which is a part of the stock-in-trade of the assessee and cannot, therefore, be regarded as income, as the amounts received by the assessee in CIT and Excess Profits Tax v. South India Pictures Ltd [(1956) SCR 223, 228] and in CIT v. Rai Bahadur Jairam Valji [(1959) 35 ITR 148 : (1959) SCR Supp 110] had been held to be. Nor

can this amount be said to have been paid as compensation for the cancellation or cessation of the managing agency of the assessee firm, for the managing agency continued and, therefore, the decision of the Judicial Committee of the Privy Council in CIT v. Shaw Wallace and Co. [(1932) LR 59 IA 206] cannot be invoked. It is, however, urged that for the purpose of rendering the sum paid as compensation to be regarded as a capital receipt, it is not necessary that the entire managing agency should be acquired. If the amount was paid as the price for the sterilisation of even a part of a capital asset which is the framework or entire structure of the assessee's profit making apparatus, then the amount must also be regarded as a capital receipt, for, as said by Lord Wrenbury in Glenboig Union Fireclay Co. Ltd. v. IRC [(1922) 12 TC 427] "what is true of the whole must be equally true of part"— a principle which has been adopted by this Court in CIT v. Vazir Sultan and Sons [Civil Appeal No. 346 of 1957, decided on March 20, 1959;(1959) 36 ITR 175] . The learned Attorney-General, however, contends that this case is not governed by the decisions in Shaw Wallace's case [(1932) LR 59 IA 206] or Vazir Sultan and Son case [Civil Appeal No. 346 of 1957, decided on March 20, 1959;(1959) 36 ITR 175] because in the present case there was no acquisition of the entire managing agency business or sterilisation of any part of the capital asset and the business structure or the profit-making apparatus, namely, the managing

agency, remains unaffected. There is no destruction or sterilisation of any part of the business structure. The amount in question was paid in consideration of the assessee firm agreeing to continue to serve as the managing agent on a reduced remuneration and, therefore, it bears the same character as that of remuneration and, therefore, a revenue receipt. We do not accept this contention. If this argument were correct, then, on a parity of reasoning, our decision in Vazir Sultan and Sons case [Civil Appeal No. 346 of 1957, decided on March 20, 1959;(1959) 36 ITR 175] would have been different, for, there also the agency continued as before except that the territories were reduced to their original extent. In that case also the agent agreed to continue to serve with the extent of his field of activity limited to the State of Hyderabad only. To regard such an agreement as a mere variation in the terms of remuneration is only to take a superficial view of the matter and to ignore the effect of such variation on what has been called the profit-making apparatus. A managing agency yielding a remuneration calculated at the rate of 20 per cent of the profits is not the same thing as a managing agency yielding a remuneration calculated at 10 per cent of the profits. There is a distinct deterioration in the character and quality of the managing agency viewed as a profit-making apparatus and this deterioration is of an enduring kind. The reduced remuneration having been separately provided, the sum of Rs 7,50,000 must be regarded as

having been paid as compensation for this injury to or deterioration of the managing agency just as the amounts paid in Glenboig case [(1922) 12 TC 427] or Vazir Sultan case [Civil Appeal No. 346 of 1957, decided on March 20, 1959;(1959) 36 ITR 175] were held to be. This is also very nearly covered by the majority decision of the English House of Lords in Hunter v. Dewhurst [(1932) 16 TC 605] . It is true that in the later English cases of Prendergast v. Cameron [(1940) 23 TC 122] and Wales Tilley [(1943) 25 TC 136] the decision in Hunter v. Dewharst [(1932) 16 TC 605] was distinguished as being of an exceptional and special nature but those later decisions turned on the words used in Rule 1 of Schedule E. to the English Act. Further, they were cases of continuation of personal service on reduced remuneration simpliciter and not of acquisition, wholly or in part, of any managing agency viewed as a profit-making apparatus and consequently the effect of the agreements in question under which the payment was made upon the profit making apparatus, did not come under consideration at all. On a construction of the agreements it was held that the payments made were simply remuneration paid in advance representing the difference between the higher rate of remuneration and the reduced remuneration and as such a revenue receipt. The question of the character of the payment made for compensation for the acquisition, wholly or in part, of any managing

agency or injury to or deterioration of the managing agency as a profit-making apparatus is covered by our decisions hereinbefore referred to. In the light of those decisions the sum of Rs 7,50,000 was paid and received not to make up the difference between the higher remuneration and the reduced remuneration but was in reality paid and received as compensation for releasing the company from the onerous terms as to remuneration as it was in terms expressed to be. In other words, so far as the managed company was concerned, it was paid for securing immunity from the liability to pay higher remuneration to the assessee firm for the rest of the term of the managing agency and, therefore, a capital expenditure and so far as the assessee firm was concerned, it was received as compensation for the deterioration or injury to the managing agency by reason of the release of its rights to get higher remuneration and, therefore, a capital receipt within the decisions of this Court in the earlier cases referred to above."

In ***Senairam Doongarmall's*** case supra, the Apex Court held as under:

"This appeal which has been filed with a certificate under section 66A(2) granted by the High Court of Assam against its judgment and order dated March 29, 1955, concerns the assessment of the appellants, a Hindu undivided family, for the assessment year 1945-1946 and 1946-1947.

The appellants owned a tea garden called the Sewpur Tea Estate in Assam. They had on the estate factories labour quarters staff quarters, etc. On February 27, 1942, the military authorities requisitioned all the factory buildings, etc., under rule 79 of the Defence of India Rules. Possession was taken sometime between March 1 and March 8, 1942. The tea garden was however left in the possession of the appellants. The possession of the military continued till the year 1945, and though the appellants looked after their tea garden, the manufacture of tea was completely stopped. Under the Defence of India Rules, the military authorities paid compensation. For the year 1944, corresponding to the assessment year 1945-1946 they paid a total sum of Rs. 2,22,080 as compensation including a sum of Rs. 10,000 for repairs to quarters for labourers and Rs. 144 which represented the assessor's fee. For the year 1945, corresponding to the assessment year 1946-1947, the military authorities paid a sum of Rs. 2,46,794 which included a sum of Rs. 15,231 for other repairs. The sums paid for repairs appear to have been admitted as paid on capital account and rightly so. The question was whether the two sums paid in the two years minus these admitted sums, or any portion thereof were received on revenue or capital account.

The assessments for the two years were made by different Income- tax Officers. For the assessment year 1945-1946 the Income-tax Officer deducted from Rs. 2,22,080, a sum of Rs. 1,03,000 on account of admissible expenses. He then applies to the balance, Rs. 1,17,080, rule 24 of the Indian Income-tax Rules, 1922, and brought to tax 40 per cent. of that sum amounting to Rs. 46,832. The assessment was made under section 23(4). For the assessment year 1946-47, the assessment was made under section 23(3) of the Income-tax Act. The Income-tax Officer excluded the sum paid on account of repairs and treated the whole of the amount as income taxable under the provisions of the Income-tax Act, after deduction of admissible expenditure. The appeals filed by the appellants to the Appellate Assistant Commissioner against both the assessments were unsuccessful. On further appeal, the Income-tax Appellate Tribunal (Calcutta Bench) was divided in its opinion. The Judicial Member held that the receipts represented revenue but on account of "use and occupation" of the premises requisitioned. He, therefore computed the net compensation attributable to such use and occupation at 20 per cent. of the total receipts in both the years. He, however, observed that if the receipts included income from the tea estate he would have been inclined to apply rule 24 in the same way as the first Income-tax Officer. The Account Member was of the opinion that the appellants were liable to pay tax on 40 per cent. of their receipts in both

the years after deduction of the sums paid for repairs of buildings and the admissible expenditure. He accepted the estimate of expenditure for the account year 1944, at Rs. 1,05,000, and directed that the admissible expenditure for the succeeding year be determined and deducted before the application of rule 24.

It appears that through some inadvertence these two orders, which were not unanimous were sent to the appellants and the Department. The Commissioner of Income-tax filed an application under section 66(1) for a reference, while the appellants filed an application under section 35 for rectification of the orders since many other matters in appeal were not considered at all. When these two applications came before the Tribunal, it was realised that the matter had to go to a third member for setting the difference. The President then heard the appeal and agreed with the Accountant Member. Though he expressed a doubt whether the appellants were entitled to the benefit of rules 23 and 24,he did not given an opinion because this point was not referred to him.

The Tribunal then referred the case to the High Court of Assam on the following two questions:

"(1) Whether the sums of Rs. 2,12,080 and Rs. 2,31,563 paid by the Government to the assessee in 1945 and 1946 respectively (exclusive of the sums paid specifically for building repairs) were revenue receipts in the hands of the assessee comprising any element of income?

(2) If so, whether the whole of the said sums less the expenses incurred by the assessee in tending the tea bushes constituted agricultural income in his hands exempt from tax under the Indian Income- tax Act, 1922?"

The reference was heard by Sarjoo Prasad, C.J., and Ram Labhaya, J., along with two writ petitions which had also been filed. They delivered separate judgments, but concurred in their answers. The High Court answered both the question against the appellants. The writ petitions were also dismissed.

Before we deal with this appeal, we consider it necessary to state at this stage the method of calculation of compensation adopted by the military authorities. It is not necessary to refer to both the years, because what was done in the first year was also done in the following year except for the change in the amounts. This method of calculation is taken from the order of the Judicial Member and is as follows:

		Rs.	a.	p.
Crop—2,11,120 1bs. at 17.85 d (half) and at 18.35 d (half)		2,12.292	14	0
15,480 1bs. at Rs. 0-11-10		11,449	12	0
52,600 1bs. at Rs. 0-15-6		50,956	4	0
		2,74,698	14	0
Less—Saving of plucking and manufacturing:				
		Rs.		
(a) Expenses at annas 3 per 1b.	…	49,209		
(b) Sale of export rights 1,32,935 1bs.	…	4,924		
(c) Purchase of export rights	…	1,629		

78,185 1bs. at annas 4			
(d) Food and clothing … 7,000 concessions …	62,762	0	0
	2,11,936	0	0
Add—For fees of assessors Rs. … …			
144 Coolie lines repairs Rs. 10,000 …	10,144	0	0
	2,22,080	0	0

From the admitted facts which have been summarized above, it is clear that the business of the appellants as tea-growers and tea-manufacturers had come to stop. The word "business" is not defined exhaustively in the Income-tax Act, but it has been held both by this court and the Judicial Committee to denote an activity with the object of earning profit. To say that a business is being carried on, means no more than that profit is to be earned by a process of production. The business of a tea-grower and manufacturer is not merely to grow tea plants but to collect tea leaves and render them fit for sale. During the years in question, the appellants were tending their teagarden to preserve the plants, but this activity cannot be described as a continuation of the business, which had come to an end for the time being. It would have hardly made any difference to the carrying on of business, if instead of the factories and buildings, the garden was requistioned and occupied, because in that event also, the business would have come to a standstill.

The compensation which was paid in the two years was no doubt paid as an equivalent of the likely profits

in those years; but as pointed out by Lord Buckmaster, in Glenboig Union Fireclay Co. Ltd. v. Commissioners of Inland Revenue and affirmed by Lord Macmillan in Van den Berghs Ltd. v. Clark**, "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 the application of that test." This proposition is as sound as it is well-expressed, and has been followed in numerous cases under the Indian Income-tax Act and also by this court. It is the quality of the payment that is decisive of the character of the payment and not the method of the payment or its measure, and makes it fall within capital or revenue.*

We are thus required to determine what was it that was paid for, or in other words what did the two payments replace if they replaced anything. The arguments at the Bar followed the pattern which has by now become quite familiar to courts. We were taken to the 12th volume of the Tax Cases series, where are collected cases dealing with excess profits duty and corporation profits tax in England following the First World War, and to other English case reported since. These cases have been considered and applied on more than one occasion by this court and we were referred to those cases as well.

Now, it is necessary to point out that the English cases were decided under a different system of taxation and must be read with care. A case can only be

decided on its own facts, and the desire to base one's decision on another case in which the facts appear to be near enough sometimes leads to error. It is well to remember the wholesome advice given by Loar Dunedin in Green v. Gliksten & Son Ltd.,[1929] 14 Tax. Cas.364 that "in these Income Tax Act cases one has to try as far as possible to tread a narrow path because there are quagmires on either side into which one can easily be led ...."*

The English cases to which we were referred were used even in England by Lord Macmillan in Van den Berghs' case (1935) 3 ITR (Eng.Cas.) 17 as mere illustrations and when cited before the Judicial Committee in Commissioner of Income-tax v. Shaw Wallace & Co.(1932) LR 59 IA 206 were put aside by Sir George Lowndes with this observation:

".....their Lordships would discard altogether the case law which has been so painfully evolved in the construction of the English income tax statutes—both the cases upon which the High Court relied and the flood of other decisions which has been let loose in this Board."

Most of the case cited before us deal with excess profits duty and corporation profits tax. In the former group, pre-war profit had to be determined, so that they might be compared with post-war business for the purpose of arriving at the excess profits, if any. In dealing with the pre-war profits, diverse receipts were considered from the angle whether they formed capital or revenue items. The observations which have been made are sometimes appropriate to the nature of the

business to which the case related and the quality of the payment in relation to that business. Similarly the corporation profits tax was a tax intended to be imposed upon the profits of British companies (which included some other corporate bodies) carrying on tread or business including the business of investments. The profits which were taxed under section 52 of the English Finance Act were required to be determined according to the principles laid down in that Act.

It is thus obvious that though the English cases may be of some help in an indirect way by focusing one's attention on what is to be regarded as relevant and what rejected they cannot be regarded in any sense as precedents to follow. Since this court on other occasions used these cases as an aid, we shall prefer to them briefly; but we have found it necessary to sound a warning because the citation of these authorities has occasionally outrun their immediate utility.

We begin with the oft-cited case of Glenboig Union Fireclay Co. Ltd's case supra. That was a case under the excess profits duty. The facts are so well-known that we need not linger over them. A seam of fireclay could not be worked and compensation was paid for it. That the clay was capital asset was indisputable, and the portion lost was a slice of capital. The hole made in the capital was filled up by the compensation paid. It was said that a portion of the capital asset was sterilised and destroyed, and even though the business

went on, the payment was treated as on capital account. The case cannot be used as precedent because here no doubt the factories and buildings were a part of fixed capital, but the payment was not so much to replace them in the hands of the appellants as to compensate them for the stoppage of business. The Glenboig case does not apply.

The case of Short Bros. Ltd. v. Commissioners of Inland Revenue – (1927) 12 Tax.Cas.955, another case under the excess profits duty illustrates a contrary principle. The company had agreed to build two ships but the contracts were cancellation and ? 100,000 was paid for cancellation of the contracts. This was held to be a receipt in the ordinary course of the company's trade. Rowlatt, J., said that it was "simply a receipt in the course of a going business, from that going business—nothing else". In the Court of Appeal, Lord Hanworth, M.R., affirmed the decision, observing:

> *"Looked at from this (business) point of view it appears clear that the sum received was received in ordinary course of business and that there was not in fact any burden cast upon the company not to carry on their trade. It was not truly compensation for not carrying on their business: it was a sum paid in ordinary course in order to adjust the relation between the shipyard and their customers."*

The payment was by a customer to the shipyard. Whether the amount was paid for ships built or because the contract was cancelled it was business receipt and in the course of the business. In the present case, the payment is not of this character, and short Bros.' Case supra does not apply.

*The next case—also of excess profits duty—is Commissioners of Inland Revenue v. Newcastle Breweries Ltd.*** In that case, the Admiralty took over one-third stock of rum of the brewery and paid to the company the cost plus 1s. per proof gallon. Later the compensation was increased by an amount of ? 5,309 and was brought to tax in the earlier year when the original compensation was paid. The observations of Rowlatt, J., though made to distinguish the case from one in which the compensation is paid for destruction of business are instructive. We shall refer to them later. The learned Judge held that this was a case of compulsory sale of rum, and that a compulsory sale was also a sale. The receipt was held to be a profit. The decision was affirmed by the Court of Appeal. This case also so far as its facts go, was very different and the actual decision has no relevance.*

*Commissioners of Inland Revenue v. Northfleet Coal and Ballast Co. Ltd. was a case like Short Bros.' Case**. ? 3000 in a lump sum were*

(1922) 12 Tax Cas. 427. **(1927) 12 Tax Cas. 955. *(1927) 12 Tax Cas. 927. #(1927) 12 Tax Cas. 1102.*

paid to be relieved from a contract, and as the business was a going business, it was held to be profit. In fact, Short Bros. Case was applied.*

*Ensign Shipping Co. Ltd. v. Commissioners of Inland Revenue**, a case of excess profits duty is interesting. During the Coal Strike of 1920, two ships of the company were ready to sail with cargoes of coal.*

*They were detained for 15 and 19 days respectively by orders of Government. In April, 1924, ? 1,078 were paid as compensation and were held to be trading receipts. Rowlatt, J., laid down that if there was an operation which produced income it was none the less taxable, because it was a compulsory operation. The learned judge then observed that he could not hold that this was a case of hire, like Sutherland v. Commissioners of Inland Revenue*** because the ships lay idle and their use was interrupted. The learned Judge then concluded:*

> *"Now it is quite clear that if a source of income is destroyed by the exercise of the paramount right….and compensation is paid for it, that is not income, although the amount of the compensation is the same as the total of the income that has been lost….but in this case I have got to decide the case of temporary interference…. Here these ships remained as ships of the concern….they merely could not sail for a certain number of days, and in lieu of the value of the use which they would have been to their owners in their profitearning capacity during those days, in lieu of that receipt, this money was paid to the owners, although they were not requisitioned, as if requisitioned….I think I ought to regard this sum, as the Commissioners have obviously regarded it, as a sum paid which to the shipowners stands in lieu of the receipts of the ship during the time of the interruption."*

This decision was approved by the Court of Appeal. Now, the case was one of loss of time during which the ships would have been usefully and profitably employed. It was argued in the Court of Appeal with the assistance of the Glenboig case# and it was suggested that the vessels were "sterilised" for the period of detention. Lord Hanworth said that was rather a

metaphorical word to use, and that the correct way was to look at the matter differently. The Master of the Rolls observed:

"But in the present case it seems to me that, looked at from a business point of view, all that has happened is that the two vessels arrived much later at the ports to which they were consigned than they would have done, with the consequent result that for the certain number of days which they were late they could not possibly make any

(1927) 12 Tax Cas. 955. **(1927) 12 Tax Cas. 1169. *(1918) 12 Tax Cas. 63. #(1922) 12 Tax Cas. 427.*

earnings, and it is in respect of that direct loss by reason of the interference with the rights exercised on behalf of His Majesty that they made a claim and have been paid compensation."

This ruling was strongly relied upon by the Department as one which laid down a principle applicable here. We do not agree. The payment there was made towards loss of profits of a going business, which was not destroyed. As a source of income, the business was intact, and the business instead of being worked for the whole period, was worked for period less by a few days and the profit of that period was made up. That may be true of one is going to determine standard profits of a particular period, because what is paid goes to profits in the period but is of no significance in a case like the present, where during the whole of the year no business at all was done nor

profits made. This case also does not help to solve the problem.

Charles Brown & Co. v. Commissioners of Inland Revenue is yet another case of excess profits duty. In that case, the business of the taxpayer was carried on under the control of the Food Controller from 1917 to 1921, and he was compelled to buy and sell at prices fixed by the Controller. By agreement a "mill standard" was fixed, and the taxpayer was allowed to retain profits up to that standard, and if there was shortfall, it was to be made up by the Controller. This amount which the taxpayer retained together with the amount paid towards shortfall was regarded as profits. The principle applicable is easily discernible. There can be little doubt that the trade was being carried on, and what was received was rightly treated as profits. Rowlatt. J., observed that this was a clearer case than the Ensign case**. The matter was covered by section 38 of the Finance (No. 2) Act of 1915, Fourth Schedule, Part 1(1), where the words were "The profits shall be taken to be the actual profits arising in the accounting period."*

*In Barr Crombie & Co, Ltd. v. Commissioners of Inland Revenue***, the company's business consisted almost entirely of managing shipping for another company. When the shipping company went into liquidation, a sum was paid as compensation to the managing company. It was held that this was a capital receipt. The reason for holding thus was that the*

structure of the managing company's whole business was affected and destroyed, and this was not profit but compensation for loss of capital. Kelsall Parsons & Co. v. Commissioners of Inland Revenue#, to which we shall refer presently, was distinguished on the ground that, though in that case the agency was cancelled, the payment was for one year and that too, the final year. This case is important is one respect, and it

(1929) 12 Tax Cas. 1256. **(1927) 12 Tax Cas. 1169. *[1947] 15 I.T.R. (Suppl.) 56. #(1938) 21 Tax Cas. 608.*

is that if the entire business structure is affected and destroyed, the payment may be regarded as replacing capital, which is lost.

These are cases of excess profits duty where profits for a particular period had to be determined and also the character of the payments in relation to the kind of business, to determine whether to treat them as excess profits or not. In the Glenboig case(1), the payment was not regarded as profit, because it replaced lost capital and so also, in the Barr Crombie case(2). These form the first group. The Short Bros. case(3), the Northfleet case(4) and Ensign Shipping Co.'s case(5), were of a going business, and what was paid was towards lost profits in a going concern. These form the second group. Newcastle Breweries' case(6) and Charles Brown and Co.'s case(7) were of business actually done and profits therefrom. None of these rulings is directly in point. In the case with which we are

concerned, the payment was not towards any capital asset to attract the first group, there was not going business so as to attract the second, and nothing was brought nor any business done with the taxpayer to make the third group applicable.

We shall next see some cases which involved corporation profits tax. In Gloucester Railway Carriage and Wagon Co. Ltd. v. Commissioners of Income Tax(8), the company was doing business of selling wagons and of hiring them out. The company then sold all the wagons which it was using for purposes of hiring. The receipt was treated as profit of trade, there being but one business and the wagons being the stock-intrade of that business. In Green v. Gliksten & Son Ltd.(9) stocks of timber were destroyed. Their written down value was ? 160,824 but the insurance company paid ? 477,838. The House of Lords held that the timber, though burnt, was realised, and that the excess of the sum over the written down book value must be brought into account. These two cases throw no light upon the problem with which we are faced, and any observations in them are so removed from the facts of this case as to be of no assistance.

The cases under Schedule D of the Income Tax Act like Burmah Steamship Co. Ltd. v. Commissioners Inland Revenue(10), a case of late delivery of ships sent for overhaul, Greyhound Racing Association (Liverpool) Ltd. v. Cooper(11), which was a case of

surrender of an agreement in which the amounts were treated as trading receipts, are

(1)(1922) 12 Tax Cas. 427. (2)[1947] 15 I.T.R. (Suppl.) 56. (3)(1927) 12 Tax Cas. 955. (4)(1927) 12 Tax Cas. 1102. (5)(1927) 12 Tax Cas. 1169. (6)(1927) 12 Tax Cas. 927. (7)(1929) 12 Tax Cas. 1256. (8)(1925) 12 Tax Cas. 720. (9) (1929) 14 Tax Cas. 364. (10)(1930) 16 Tax Cas. 67. (11)(1936) 20 Tax Cas. 373.

not cases of stoppage of a business and are not relevant. Kelsall Parsons' case, where one of the agreements of a commission agency which was to run for 3 years was terminated at the end of the second year and compensation of ? 1,500 was paid for the last and final year, was held on its special facts to involve taxable profits of trading. Though the business came prematurely to an end, the structure of the business was not affected because the payment was in lieu of profits in the final year of the business as if business had been done. The payment was held to be within the structure of the business in the same way as in Shove v. Dura Manufacturing Co. Ltd.** The converse of these cases is the well-known Van den Berghs Ltd. v. Clark***, where mutual trade agreements were rescinded between two companies and ? 450,000 were paid to the assessee company as "damages". This was treated as capital receipt and not and income receipt to be included in computing the profits of trade under*

Schedule D, Case 1, of the Income Tax Act of 1918. Lord Macmillan observed:

> *"On the contrary the cancelled agreements related to the whole structure of the appellants' profit-making apparatus. They regulated 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, 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."*

We have referred to these cases to show that none of them quite covers the problem before us. The facts are very dissimilar, and the observations, though attractive, cannot always be used with profit and often not without some danger of error. We shall now turn to the cases of this court, which were referred to at the hearing.

The first case of this court is Commissioner of Income-tax v. South India Pictures Ltd.# The South India Pictures Ltd. held distribution rights for 5 years of three films towards the completion of which they had advanced money to a film producing company, called the Jupiter Pictures. When the term had partially run out, the agreement for distribution was cancelled, and the South India Pictures Ltd. received Rs. 26,000 as commission. The question was whether this sum was on capital or revenue account. Das, C.J., and Venkatarama Aiyar, J., held that it was the latter, while Bhagwati, J., held that it was the former. The Learned Chief Justice came to his conclusion on four grounds:

(i) that the payment was towards commission which would

(1938) 21 Tax Cas. 608. **(1941) 23 Tax Cas. 779. *(1935) 3 I.T.R. (Eng. Cas.) 17. #[1956] 29 I.T.R. 910.*

have been earned; (ii) that it was not the price of any capital asset sold, surrendered or destroyed; (iii) that the structure of the business, which was a going business, was not affected; and (iv) that the payment was merely an adjustment of the relation between the South India Pictures Ltd. and the Jupiter Pictures. The Learned Chief Justice thus rested his decision on Short Bros.' and Kelsall Parsons'** cases and not upon Van den Berghs'*** or Barr Crombie's# case.*

Bhagwati, J., who dissented, judged the matter from the angle of business accountancy. He observed that money advanced to produce the cinema pictures, it returned, would have been credited on the capital side as a return of capital, just as expenditure for distribution work was revenue expenditure and the commission, a revenue receipt. On a purity of reasoning, the learned judge held that money spent in acquiring distribution rights was a capital outlay, and that when distribution rights were surrendered, it was capital which was returned, since the agreement was a composite one, the films were a capital asset and the payment for their release was a return of capital.

With due respect, it is difficult to see how the payment could be regarded as capital in that case. The fact which seems to have been overlooked in the

minority view was that the entire capital outlay had, in fact, been previously recouped and even the security held by the South India Pictures had been extinguished. It was a portion of the running business which ceased to be productive of commission and by the payment, the commission which would have been earned and would have constituted a revenue receipt when so earned, was put in the pockets of the South India Pictures. The business of the South India Pictures was still a going business, one portion of which instead of being fruitful by stages became fruitful all at once. What was received was still the fruit of business and thus revenue. The case, though interesting, is difficult to apply in the present context of facts, where no business at all done and what was received was not the fruit of any business.

The next case of this court, Commissioner of Income-tax v. Rai Bahadur Jairam Valji##, may be seen. The assessee there was a contractor, and received Rs. 2,50,000 as compensation for premature termination of a contract. This was held to be a revenue receipt. The assessee had many businesses including many contracts, and the receipt was considered as one in the ordinary course of business. All the English decisions to which we have referred were examined in search for principles, but

(1927) 12 Tax Cas. 955. **(1938) 2 Tax Cas. 608. *(1935) 3 I.T.R. (Eng. Cas). 17. #[1947] 15 I.T.R. (Suppl.) 56. ##[1959] 35 I.T.R. 148.*

the principle on which the decision was rested was that the payment was an adjustment of the rights under the contract and must be referred to the profits which could be made if the contract had instead been carried out. The payment not being on account of capital outlay and the assessee not being prevented from carrying on his business, the receipt was held to be revenue, that is to say, related to income from a contract terminated prematurely. In a sense, the case is analogous to the South India Pictures Ltd. Case which it follows.*

*In Commissioner of Income-tax v. Vazir Sultan & Sons**, the assessee held the sole selling agency and distribution rights of a particular brand of cigarette in the Hyderabad State on foot of a 2 per cent. discount on all business done. Subsequently, the area outside Hyderabad State was also included on the same terms. Later still, the area was again reduced to the Hyderabad State. Rs. 2,19,343 were paid by way of compensation "for loss of territory outside Hyderabad". Bhagwati, J., and Sinha, J. (as he then was), held that the compensation was on capital account, while Kapur, J., held otherwise. The reason given by the majority was that the agency agreement was a capital asset and the payment was in lieu of the loss of a portion of the capital asset. Kapur, J., on the other hand, held that the loss which was replaced was the loss of agency commission and bore its character. The case furnishes a difficult test to apply. If what was adjusted was the relationship between the parties and if there was a*

going business as, in fact, there was, the case comes within the dicta in the South India Pictures Ltd. Case and Jairam Valji's case***. The case can only be a decision on the narrow ground that a portion of the "fixed capital" was lost and paid for.*

In Godrej & Co. v. Commissioner of Income-tax#, the assessee firm, which held a managing agency, released the managed company from an onerous agreement and in consideration was paid Rs. 7,50,000. It was held that the payment was not made to make up the difference in the remuneration of the managing agency firm but to compensate it for the deterioration or injury of an enduring kind to the managing agency itself. The injury being thus to a capital asset, the compensation paid was held to be on capital account.

The last case of this court to which reference may be made is Commissioner of Income-tax v. Shamsher Printing Press##. That was a very special case. There, the premises of the press were requisitioned by Government, but the press was allowed to set up its business

[1956] 29 I.T.R. 910. **[1959] 36 I.T.R. 175. *[1959] 35 I.T.R. 148. #[1959] 39 I.T.R. 381. ##[1960] 39 I.T.R. 90.*

elsewhere, the charges for shifting the machines, etc., being paid by Government. In addition, Government paid a sum claimed as loss of profits, which was expected to bring up the profits to the level of profits while the business was in its old place. The

assessee claimed that this sum was paid as compensation for loss of goodwill arising from its old locality. there was, however, nothing to show that the payment was for goodwill, and it was held that the compensation paid must be regarded as money arising as profits in the course of business. It was like putting money in the till to bring the profits actually made to the level of normal profits.

All these cases were decided again on their special facts. Though they involved examination of other decisions in search for the true principles, it cannot be said that they resulted in the discovery of any principle of universal application. To summarise them: South India Pictures' case was so decided because the money received was held to be in lieu of commission which would have been earned by the business which was still going, and the receipt was treated as the fruit of business. The same reason was given in Jairam Valji's case**, and the Shamsher Printing Press case***. In Vazir Sultan's case#, the compensation was held to replace loss of capital, and in Godrej's case##, the compensation was said not to have any relation to the likely income or profits but to loss of capital. Each case was thus decided on its facts.*

We have so far shown the true ratio of each case cited before us, and have tried to demonstrate that these cases do no more stimulate the mind, but none can serve as a precedent, without advertence to its facts. The nature of the business, or the nature of the

outlay or the nature of the receipt in each case was the decisive factor, or there was a combination of these factors. Each is thus an authority in the setting of its own facts.

Before we deal with the facts of this case and attempt to answer the question on which there is so much to guide but nothing to bind, we will refer to two cases of the Judicial Committee, one of which is Commissioner of Income-tax v. Shaw Wallace & Co.###, to which we have referred in another connection. In that case, all the authorities prior to 1935 to which we have referred (and some more) were used in aid of arguments; but the Judicial Committee, for reasons which are now illustrated by this judgment, declined to comment on them. Shaw Wallace and Co. did many business, and included in them was the

[1956] 29 I.T.R. 910. **[1959] 35 I.T.R. 148. *[1960] 39 I.T.R. 90. #[1959] 36 I.T.R. 175. ##[1959] 37 I.T.R. 381. ###[1932] L.R. 59 I.A. 206.*

managing agency of two oil-producing companies. This agency was terminated, and compensation was paid for it. The usual question arose about capital or revenue. The Full Bench of the Calcutta High Court related the payment of goodwill, but the Judicial Committee rejected that ground because no goodwill seemed to have been transferred. The Judicial Committee also rejected the contention that it was compensation in lieu of notice under section 206 of the Indian Contract Act, as there was no basis for it either.

The Judicial Committee held that income meant a periodical monetary return coming in with some sort of regularity or expected regularity from a definite source and in business was the produce of something "Loosely spoken of as capital". In business, income is profit earned by a process of production, or, in other words, by the continuous exercise of an activity. In this sense, the sum sought to be charged could not be regarded as income. It was not the product of business but some kind of solatium for not carrying on business and thus not revenue.

The case is important inasmuch as this analysis of "income" has been accepted by this court and has been cited with the further remark made in Gopal Saran Narain Singh v. Commissioner of Income-tax, that the words "profits and gains" used in the Indian Income-tax Act do not restrict the meaning of the word "income" and the whole expression is "income" writ large. From this case, it follows that the first consideration before holding a receipt to be profits or gains of business within section 10 of the Indian Income-tax Act is to see if there was a business at all of which it could be said to be income.*

We shall now take up for consideration the facts of our case, and see how far any principle out of the several which have governed earlier cases can be usefully applied. The assessee was a tea-grower and tea manufacturer. His work consisted in growing tea and in preparing leaves by a manufacturing process

into a commercial commodity. The growing of tea plants only furnished the raw material for the business. Without the factory and the premises, the tea leaves could not be dried, smoked and cured to become tea, as is known commercially, and it could not be packed or sold. The direct and immediate result of the requisition of the factories was to stop the business. That the tea was grown or that the plants were tended did not mean that the business was being continued. It only meant that the source of the raw material was intact but the business was gone.

*Now, when the payment was made to compensate the assessee, no doubt the measure was the out-turn of tea which would have been manufactured; but that has little relevance. The assessee was not *[1935] L.R. 62 I.A. 207. compensated for loss or destruction of or injury of a capital asset. The buildings were taken for the time being, but the injury was not so much to the fixed capital as to the business as a whole. The entire structure of business was affected to such an extent that no business was left or was done in the two years. This was not a case where the interruption was caused by the act of a contracting party so that the payment could be regarded as an adjustment of a contract by payment. It was a case of compulsory requisition, but the requisition did not involve the buying of tea either as raw material or even as a finished product. If that had been the case, it might have been possible to say that since business was done, though compulsorily, profits*

had resulted. It was not even a case in which the business continued, and what was paid was to bring up the profits to normal level. the observations of Rowlatt, J., in Newcastle Breweries' case, distinguish a case where business is carried on and one in which business comes to an end. The learned Judge observes:*

> *"Now I have no doubt that a Government requisition, such as took place during the war, could destroy a trade, and anything which was paid would be compensation for such destruction. I can understand, for instance, if they had requisitioned in this case the people's building and stopped them either brewing and selling or doing anything else, and paid a sum, that could not be taken as a profit; they would have destroyed the trade pro tempore and paid compensation for that destruction; and in fact I dare say if they take the whole of the raw materials of a man's trade and prevent him carrying it on, and pay a sum of money, that is to be taken, not as profit on the sale of raw materials, which he never would have sold, but as compensation for interfering with the trade altogether."*

These observations, though made under a different statute, are, in general, true of a business as such, and can be usefully employed under the Indian Income-tax Act. Our Act divides the sources of income, profits and gains under various heads in section 6. Business is dealt with under section 10, and the primary condition of the application of the section is that tax is payable by an assessee under the head "profits and gains of a business" in respect of a business carried on by him. Where an assessee does not carry on business at all, the section cannot be made applicable, and the compensation that he receives cannot bear the character of profits of a business. It is for this reason

*that the Judicial Committee in Shaw Wallace's case** observed that the compensation paid in that case was not the product of business, or, in other words, profit, but some kind of solatium for not carrying on*

(1927) 12 Tax Cas. 927.[1932] L.R. 59 I.A. 206.*

business and thus, not revenue. It is to be noted that Das, C.J., in South India Pictures' case, in distinguishing Shaw Wallace's case**, made the following observation:*

*"In Shaw Wallace's case**, the entire distributing agency work was completely closed, whereas the termination of the agreements in question did not have that drastic effect on the assessee's business at all.....In Shaw Wallace's case**, therefore, it could possibly be said that the amount paid there represented a capital receipt."*

*The observation is guarded, but in recognises the difference made in the Privy Council case and others between payment to compensate interference with a going business and compensation paid for stoppage of a business altogether. This distinction was emphasised in the dissenting opinion in Vazir Sultan's case***.*

Though the payment in question was not made to fill a hole in the capital of the assessee, as in the Glenboig case#, nor was it made to fill a hole in the profits of a going business as in the Shamsher Printing Press case##, it cannot be treated as partaking the character of profits because business not having been done, no question of the profits taxable under section 10 arose.

The Privy Council described such a payment as a solatium. It is not necessary to give it a name; it is sufficient to say that it was not profit of a business.

Once it is held that this was not profit at all, it is clear that rules 23 and 24 of the Indian Income-tax Rules could not apply, and there was no question of apportioning the amount, as laid down in rule 24. The whole of the amount received by the assessee was not assessable.

It remains to consider whether the payment could be treated as income from property under section 9 of the Income-tax Act. That this was never the case of the Department is clear from the fact that the income was not processed under that section, and even the Judicial Member of the Tribunal, who entertained this opinion, did not express it as his decision in the case. This aspect of the matter not having been considered in the case before, we cannot express any opinion upon it.

In our opinion, the answer to the two questions ought to have been:

Question (1): No.

Question (2): Does not arise.

In the result, the appeal is allowed with costs here and in the High Court.

Appeal allowed."

In ***Saurashtra Cement's*** case supra, the Apex Court held as under:

"16. In Kettlewell Bullen and Co. Ltd. [AIR 1965 SC 65] dealing with the question whether compensation received by an agent for premature determination of the contract of agency is a capital or a revenue receipt, echoing the views expressed in Rai Bahadur Jairam Valji [AIR 1959 SC 291 : (1959) 35 ITR 148] and analysing numerous judgments on the point, this Court laid down the following broad principle, which may be taken into account in reaching a decision on the issue: (Kettlewell Bullen and Co. Ltd. case [AIR 1965 SC 65] , AIR p. 79, para 36)

"36. … Where on a consideration of the circumstances, payment is made to compensate a person for cancellation of a contract which does not affect the trading structure of his business, nor deprive him of what in substance is his source of income, termination of the contract being a normal incident of the business, and such cancellation leaves him free to carry on his trade (freed from the contract terminated) the receipt is revenue: where by the cancellation of an agency the trading structure of the assessee is impaired, or such cancellation results in loss of what may be regarded as the source of the assessee's income, the payment made to compensate for cancellation of the agency agreement is normally a capital receipt."

17. We have considered the matter in the light of the aforenoted broad principle. It is clear from Clause 6 of the agreement dated 1-9-1967, extracted above, that the liquidated damages were to be calculated at 0.5% of the price of the respective machinery and equipment to which the items were delivered late, for each month of delay in delivery completion, without proof of the actual damages the assessee would have suffered on

account of the delay. The delay in supply could be of the whole plant or a part thereof but the determination of damages was not based upon the calculation made in respect of loss of profit on account of supply of a particular part of the plant.

18. It is evident that the damages to the assessee were directly and intimately linked with the procurement of a capital asset i.e. the cement plant, which would obviously lead to delay in coming into existence of the profit making apparatus, rather than a receipt in the course of profit earning process. Compensation paid for the delay in procurement of capital asset amounted to sterilisation of the capital asset of the assessee as the supplier had failed to supply the plant within time as stipulated in the agreement and Clause 6 thereof came into play. The aforestated amount received by the assessee towards compensation for sterilisation of the profit earning source, not in the ordinary course of their business, in our opinion, was a capital receipt in the hands of the assessee.

19. We are, therefore, in agreement with the opinion recorded by the High Court on Questions (i) and (ii) extracted in Para 2 and hold that the amount of Rs. 8,50,000 received by the assessee from the suppliers of the plant was in the nature of a capital receipt.""

(iii) The one time voluntary compensation paid to the petitioner also cannot be treated as a salary under Section 15 of

the I.T Act or perquisite under Section 17(2)(vi) of the I.T Act; in this context, it is relevant to state that taxability would arise only when the option holder exercises its option, at which stage the market value of the allotted share and the value of the stock option is charged as perquisite in the hands of the option holder, especially when there is computational impossibility, when there is no allotment of shares as held by the Apex Court in ***Srinivasa Shetty's*** case supra as under:

> *"8. The section operates if there is a transfer of a capital asset giving rise to a profit or gain. The expression "capital asset" is defined in Section 2(14) to mean "property of any kind held by an assessee". It is of the widest amplitude, and apparently covers all kinds of property except the property expressly excluded by clauses (i) to (iv) of the sub-section which, it will be seen, does not include goodwill. But the definitions in Section 2 are subject to an overall restrictive clause. That is expressed in the opening words of the section: "Unless the context otherwise requires." We must therefore enquire whether contextually Section 45, in which the expression "capital asset" is used, excludes goodwill.*
>
> *9. Goodwill denotes the benefit arising from connection and reputation. The original definition by Lord Eldon in Crutwell v. Lye [1810, 17 Ves 335] that*

goodwill was nothing more than "the probability that the old customers would resort to the old places" was expanded by Wood V.C. in Churton v. Douglas [1859 John 174] to encompass every positive advantage "that has been acquired by the old firm in carrying on its business, whether connected with the premises in which the business was previously carried on or with the name of the old firm, or with any other matter carrying with it the benefit of the business".In Trego v. Hunt [1896 AC 7] Lord Herschell described goodwill as a connection which tended to become permanent because of habit or otherwise. The benefit to the business varies with the nature of the business and also from one business to another. No business commenced for the first time possesses goodwill from the start. It is generated as the business is carried on and may be augmented with the passage of time. Lawson in his Introduction to the Law of Property describes it as property of a highly peculiar kind. In CIT, West Bengal (III) v. Chunilal Prabhudas & Co. [(1970) 76 ITR 566 (Cal HC)] the Calcutta High Court reviewed different approaches to the concept:

"It has been horticulturally and botanically viewed as 'a seed sprouting' or an 'acorn growing into the mighty oak of goodwill'. It has been geographically described by locality. It has been historically explained as growing and crystallising traditions in the business. It has been described in terms of a magnet as the 'attracting force'. In terms of comparative dynamics, goodwill has been

described as the 'differential return of profit'. Philosophically it has been held to be intangible. Though immaterial, it is materially valued. Physically and psychologically, it is a 'habit' and sociologically it is a 'custom'. Biologically, it has been described by Lord Macnaghten in Trego v. Hunt [1896 AC 7] as the 'sap and life' of the business. Architecturally, it has been described as the 'cement' binding together the business and its assets as a whole and a going and developing concern."

A variety of elements goes into its making, and its composition varies in different trades and in different businesses in the same trade, and while one element may preponderate in one business, another may dominate in another business. And yet because of its intangible nature, it remains insubstantial in form and nebulous in character. Those features prompted Lord Macnaghten to remark in CIT v. Muller & Co.'s Margarine Limited [1901 AC 217] that although goodwill was easy to describe, it was nonetheless difficult to define. In a progressing business goodwill tends to show progressive increase. And in a failing business it may begin to wane. Its value may fluctuate from one moment to another depending on changes in the reputation of the business. It is affected by everything relating to the business, the personality and business rectitude of the owners, the nature and character of the business, its name and reputation, its location, its impact on the contemporary market, the prevailing

socio-economic ecology, introduction to old customers and agreed absence of competition. There can be no account in value of the factors producing it. It is also impossible to predicate the moment of its birth. It comes silently into the world, unheralded and unproclaimed and its impact may not be visibly felt for an undefined period. Imperceptible at birth it exists enwrapped in a concept, growing or fluctuating with the numerous imponderables pouring into, and affecting the business. Undoubtedly, it is an asset of the business, but is it an asset contemplated by Section 45?

10. Section 45 charges the profits or gains arising from the transfer of a capital asset to income tax. The asset must be one which falls within the contemplation of the section. It must bear that quality which brings Section 45 into play. To determine whether the goodwill of a new business is such an asset, it is permissible, as we shall presently show, to refer to certain other sections of the head, "Capital gains". Section 45 is a charging section. For the purpose of imposing the charge. Parliament has enacted detailed provisions in order to compute the profits or gains under that head. No existing principle or provision at variance with them can be applied for determining the chargeable profits and gains. All transactions encompassed by Section 45 must fall under the governance of its computation provisions. A transaction to which those provisions cannot be applied must be regarded as never intended by Section 45 to be the subject of the charge. This

inference flows from the general arrangement of the provisions in the Income Tax Act, where under each head of income the charging provision is accompanied by a set of provisions for computing the income subject to that charge. The character of the computation provisions in each case bears a relationship to the nature of the charge. Thus the charging section and the computation provisions together constitute an integrated code. When there is a case to which the computation provisions cannot apply at all, it is evident that such a case was not intended to fall within the charging section. Otherwise one would be driven to conclude that while a certain income seems to fall within the charging section there is no scheme of computation for quantifying it. The legislative pattern discernible in the Act is against such a conclusion. It must be borne in mind that the legislative intent is presumed to run uniformly through the entire conspectus of provisions pertaining to each head of income. No doubt there is a qualitative difference between the charging provision and a computation provision. And ordinarily the operation of the charging provision cannot be affected by the construction of a particular computation provision. But the question here is whether it is possible to apply the computation provision at all if a certain interpretation is pressed on the charging provision. That pertains to the fundamental integrality of the statutory scheme provided for each head.

11. The point to consider then is whether if the expression "asset" in Section 45 is construed as including the goodwill of a new business, it is possible to apply the computation sections for quantifying the profits and gains on its transfer.

12. The mode of computation and deductions set forth in Section 48 provide the principal basis for quantifying the income chargeable under the head "Capital gains". The section provides that the income chargeable under that head shall be computed by deducting from the full value of the consideration received or accruing as a result of the transfer of the capital asset: "(ii) the cost of acquisition of the capital asset...."

13. What is contemplated is an asset in the acquisition of which it is possible to envisage a cost. The intent goes to the nature and character of the asset, that it is an asset which possesses the inherent quality of being available on the expenditure of money to a person seeking to acquire it. It is immaterial that although the asset belongs to such a class it may, on the facts of a certain case, be acquired without the payment of money. That kind of case is covered by Section 49 and its cost, for the purpose of Section 48 is determined in accordance with those provisions. There are other provisions which indicate that Section 48 is concerned with an asset capable of acquisition at a cost. Section 50 is one such provision. So also is sub-

section (2) of Section 55. None of the provisions pertaining to the head "Capital gains" suggests that they include an asset in the acquisition of which no cost at all can be conceived. Yet there are assets which are acquired by way of production in which no cost element can be identified or envisaged. From what has gone before, it is apparent that the goodwill generated in a new business has been so regarded. The elements which create it have already been detailed. In such a case, when the asset is sold and the consideration is brought to tax, what is charged is the capital value of the asset and not any profit or gain.

14. In the case of goodwill generated in a new business there is the further circumstance that it is not possible to determine the date when it comes into existence. The date of acquisition of the asset is a material factor in applying the computation provisions pertaining to gains. It is possible to say that the "cost of acquisition" mentioned in Section 48 implies a date of acquisition, and that inference is strengthened by the provisions of Sections 49 and 50 as well as sub-section (2) of Section 55.

15. It may also be noted that if the goodwill generated in a new business is regarded as acquired at a cost and subsequently passes to an assessee in any of the modes specified in sub-section (1) of Section 49, it will become necessary to determine the cost of acquisition to the previous owner. Having regard to the nature of the asset, it will be impossible to determine

such cost of acquisition. Nor can sub-section (3) of Section 55 be invoked, because the date of acquisition by the previous owner will remain unknown.

16. We are of opinion that the goodwill generated in a newly commenced business cannot be described as an "asset" within the terms of Section 45, and therefore its transfer is not subject to income tax under the head "Capital gains".

17. The question which has been raised before us, has been considered by some High Courts, and it appears that there is a conflict of opinion. The Madras High Court in CIT v.K. Rathnam Nadar [(1969) 71 ITR 433 (Mad HC)] , the Calcutta High Court in CIT v. Chunilal Prabhudas & Co. [(1970) 76 ITR 566 (Cal HC)] , the Delhi High Court in Jagdev Singh Mumick v. CIT [(1971) 81 ITR 500 (Del HC)] , the Kerala High Court in CIT v.E.C. Jacob [(1973) 89 ITR 88 (Ker HC)] , the Bombay High Court in the CIT v. Home Industries & Co. [(1977) 107 ITR 609 (Bom HC)] and CIT v. Michel Postal [(1978) 112 ITR 315 (Bom HC)] and the Madhya Pradesh High Court in CIT v. Jaswant Lal Dayabhai [(1978) 114 ITR 798 (MP HC)] have taken the view that the receipt on the transfer of goodwill generated in a business is not subject to income tax as a capital gain. On the other side lies the view taken by the Gujarat High Court in CIT v. Mohanbhai Pamabhai [(1973) 91 ITR 393 (Guj HC)] and the Calcutta High Court in K.N. Daftary v. CIT [(1977) 106 ITR 998 (Cal HC)] that even

> *if no cost is incurred in building up the goodwill of the business, it is nevertheless a capital asset for the purpose of capital gains, and the cost of acquisition being nil the entire amount of sale proceeds relating to the goodwill must be brought to tax under the head "Capital gains". It is apparent that the preponderance of judicial opinion favours the view that the transfer of goodwill initially generated in a business does not give rise to a capital gain for the purposes of income tax."*

In the instant case, the material on record discloses that undisputedly the petitioner did not exercise his options under the subject FSOPs nor was there any allotment or transfer of shares in his favour and the subject compensation was paid to him only towards compensation for loss on reduction/diminution in the value of stock options held by the petitioner; it is significant to note that FSOPs would become taxable only under two circumstances viz., when the petitioner exercises his option and the differential amount is taxed or when the shares allotted to him are either sold or transferred, thereby becoming taxable as capital gain; as stated supra, the petitioner neither exercises his option nor sold or transferred his shares and FPS made the subject payment in favour of the petitioner only towards reduction/diminution of the

value of FSOPs and consequently, the impugned order deserves to be quashed on this ground also.

(iv) The material on record indicates that the subject one time compensatory payment made to the petitioner is in the nature of capital receipt and the same cannot be brought to tax under any other Head of income including "other sources" and Capital receipt which is not chargeable under Section 45 of the I.T.Act is not chargeable under any other head; in ***D.P.Sandhu's case supra,*** the Apex Court held as under:-

> "*13. Were it not for the inability to compute the cost of acquisition under Section 48, there is, as we have said, no doubt that a monthly tenancy or leasehold right is a capital asset and that the amount received on its surrender was a capital receipt. But because we have held that Section 45 cannot be applied, it is not open to the Department to impose tax on such capital receipt by the assessee under any other section. This Court, as early as in 1957 had, in United Commercial Bank Ltd. v. CIT [(1957) 32 ITR 688 : 1958 SCR 79] held that the heads of income provided for in the sections of the Income Tax Act, 1922 are mutually exclusive and where any item of income falls specifically under one head, it has to be charged under that head and no other. In other words, income derived from different sources falling under a specific head has to be computed for the purposes of taxation in the manner*

provided by the appropriate section and no other. It has been further held by this Court in East India Housing and Land Development Trust Ltd. v. CIT [(1961) 42 ITR 49 (SC)] that if the income from a source falls within a specific head, the fact that it may indirectly be covered by another head will not make the income taxable under the latter head. (See also CIT v. Chugandas and Co. [(1965) 55 ITR 17 : (1964) 8 SCR 332])"

In ***Cadell Weaving Mill's case supra,*** the Bombay High Court held as under:-

"*11. We find merit in the submissions advanced on behalf of the assessee. Both the parties before us have proceeded on the basis that the tenancy right is a capital asset. This is clear from the submissions advanced on both sides. Even the Tribunal has proceeded on the basis that if the tenancy right is a property, then the consideration received for transfer thereof would not be chargeable as revenue receipt. It is well-settled that all receipts are not taxable under the Income-Tax Act. Section 2(24) defines "income". It is no doubt an inclusive definition. However, a capital receipt is not income under section 2(24) unless it is chargeable to tax as capital gains under section 45. It is for this reason that under section 2(24)(vi) that the Legislature has expressly stated, inter alia, that income shall include any capital gains chargeable under section 45. Under section 2(24)(vi), the Legislature has not included all capital gains as income. It is only capital*

gains chargeable under section 45 which has been treated as income under section 2(24). If the argument of the Department is accepted then all capital gains whether chargeable under section 45 or not, would come within the definition of the word "income" under section 2(24). Further, under section 2(24)(vi), the Legislature has not stopped with the words "any capital gains". On the contrary, the Legislature has advisedly stated that only capital gains which are chargeable under section 45 could be treated as income. In other words, capital gains not chargeable to tax under section 45 fall outside the definition of the word "income" in section 2(24). It is true that section 2(24) is an inclusive definition. However, in this case, we are required to ascertain the scope of section 2(24)(vi) and for that purpose we have to read the sub-section strictly. We cannot widen the scope of sub-section by saying that the definition as a whole is inclusive and not exhaustive. In the present case, the words "chargeable under section 45" are very important. They are not being read by the Department. These words cannot be omitted. In fact, the prior history shows that capital gains were not chargeable before 1946. They were not chargeable between 1948 and 1956. Therefore, whenever an amount which is otherwise a capital receipt is to be charged to tax, section 2(24) specifically so provides. In the case of CIT v. Gulub Chand, [1991] 192 ITR 495 (All), the assessee received Rs. 15,000 as surrender value for surrendering the tenancy of a

godown occupied by the assessee as a tenant. In the return filed by him, the amount was shown as capital gains. The assessee claimed that the amount was non-taxable. The Income-Tax Officer held that the amount was taxable as a casual and non-recurring receipt under section 10(3) of the Act. The Tribunal held that the amount received was a capital gain. On a reference, it was held by the High Court that section 10(3) applied to capital receipts. That, if the amount received for surrender of the tenancy right was a capital gain but was not chargeable under section 45 then the receipt would fall under section 10(3). With respect, we do not agree with the said judgment. The Allahabad High Court has failed to read section 2(24)(vi) in its entirety. Reading section 2(24)(vi) in its entirety, it is only capital gains which are chargeable under section 45 which are included in the definition of the word "income". That, the capital gains not chargeable for any reason under section 45 cannot be brought to tax as income by applying the general connotation under section 2(24). It is for this reason that proviso (i) to section 10(3) also refers to capital gains chargeable under section 45. The said proviso uses the same phraseology as is used by section 2(24)(vi). In other words, capital gains chargeable under section 45 alone constitute income. Further, such capital gains are required to be charged and computed under the scheme of section 45 to section 55 and it is for this reason that such capital gains do not fall under section

10(3). In other words, business income, salary income, and capital gains chargeable under section 45 stand outside section 10(3) because salary income, business income and such capital gains are chargeable and computable under a different set of sections. Therefore, when the source of a receipt has a link with business income or salary income or capital gains chargeable under section 45 then section 10(3) will not apply. Hence, we respectfully do not agree with the view taken by the Allahabad High Court in Gulab Chand's case, [1991] 192 ITR 495. In the case of B.K. Roy P. Ltd. v. CIT, [1995] 211 ITR 500 (Cal), the petitioner received Rs. 21 lakhs from Shaw Wallace and Company as compensation on surrender of monthly tenancy. The tenancy was a capital asset and no cost of acquisition was incurred for its acquisition. In the assessment proceedings, the Assessing Officer accepted that the said sum could not be assessed to tax since there was no cost of acquisition of the monthly tenancy. The Commissioner, however, took the view that although the said amount was not assessable as capital gains it was assessable as casual receipts under section 10(3) by placing reliance on the judgment of the Allahabad High Court in Gidab Chand's case, [1991] 192 ITR 495. Ultimately, the matter came to the Calcutta High Court which took the view that the amount received as capital gains cannot be taxed as casual and non-recurring income. That, the judgment of the Allahabad High Court in Gulab Chand's case,

[1991] 192 ITR 495 was contrary to the judgment of the Supreme Court in the case of A. Gasper v. CIT, [1991] 192 ITR 382. That, if the contention of the Department was taken to its logical conclusion, it would mean that everything which is exempted from capital gains by the statute would become taxable as casual and non-recurring receipt. That, capital gains have been specifically dealt with under sections 45 to 55 of the Act. That, any amount received on transfer of a capital asset is liable to be taxed in accordance with the specific provisions of section 45 to section 55 of the Act and if any amount of capital gain is not taxable as capital gain for any reason, then that amount cannot be treated as a casual and non-recurring receipt under section 10(3) of the Act. That, section 10(3) does not apply to capital receipts. That, proviso (i) to section 10(3) recognises that capital gains chargeable under section 45 will not come within its ambit. That, section 10 lays down that certain categories of income will not be included in the computation of total income of a person. That, a casual receipt not exceeding. Rs. 5,000 will not be taxed. However, from this it does not follow that any capital receipt above Rs. 5,000 will have to be taxed. That, if a person receives Rs. 10,000 by way of legacy, the amount cannot be brought to tax on the ground that it is a casual and non-recurring receipt above Rs. 5,000. That/section 10 is not a charging section. That, section 10 merely excludes certain types of income from the ambit of the total income as defined

under the Act. Hence, the Calcutta High Court dissented from the view taken by the Allahabad High Court in Gulab Chand's case, [1991] 192 ITR 495. With respect, we are in agreement with the judgment of the Calcutta High Court in the case of B.K. Roy P. Ltd. v. CIT, [1995] 211 ITR 500. Mr. Desai, learned counsel for the Revenue, however, emphasised the judgment of the Supreme Court in the case of CIT v. B.C. Srinivasa Setty, [1981] 128 ITR 294. He submitted that like goodwill, statutory tenancy denotes a benefit. He contended that statutory tenancy cannot be described as an asset if there is no cost of acquisition. Therefore, he relied upon the above judgment. In the case of B.C. Srinivasa Setty's case, [1981] 128 ITR 294, the Supreme Court has held that goodwill generated in a newly commenced business cannot be described as an asset within section 45 of the Act and the transfer of the goodwill generated in a business does not give rise to a capital gain for the purposes of Income-Tax. That, goodwill denotes the benefit arising from connection and reputation. That, the charging sections and the computation provisions together constitute an integrated code and when there is a case to which the computation provisions do not apply, it is evident that such a case was not intended to fall within the charging section. Accordingly, learned counsel for the Department argued that in the case of transfer of a capital asset like tenancy where computation provisions do not apply, the Supreme

Court has laid down that such a case was not intended to fall within section 45. Hence, it was contended that if, for want of cost of acquisition, the case cannot fall under section 45 then it could still fall under section 56. According to learned counsel, therefore, the amounts received on surrender of tenancy rights if not chargeable to tax as capital, gains under section 45, they are still liable to be taxed as income from other sources. According to learned counsel, capital gains of an asset which do not have the cost of acquisition and which do not fall under section 45 can fall under section 56 of the Act. That, merely because an asset has no cost, it cannot be said that there is no capital gains and that the entire receipt represents capital receipt. It is further contended that section 14 of the Income-Tax Act shows that all capital gains constitute income. That, under section 14 the expression "capital gains" is not restricted to chargeability under section 45. We do not find any merit in this contention. The' point which arises for determination in this case did not arise in the case of B.C. Srinivasa Setty's case, [1981] 128 ITR 294 (SC). Secondly, as stated above, capital gains chargeable under section 45 alone are treated as income by the Legislature. Thirdly, statutory tenancy is held to be property by the Supreme Court. It is a real asset. It is not a self-generated asset as in the case of a goodwill. Lastly, the amendments made to the Income-Tax Act with effect from April 1, 1995, under which cost of acquisition is to be calculated as nil clearly shows

that the Act applies only to capital gains chargeable under section 45. If such gains fell under section 56 as is now sought to be contended then one fails to understand why the Legislature should have opted for a lesser incidence of tax. If capital gains fell under section 56 as is contended by the Department then such receipt would be liable to tax at the rate of 35 per cent, whereas, by the above legislative change, the receipts are made taxable at 20 per cent, under section 45. In this connection, the circular issued by the Central Board of Direct Taxes as reported in [1994] 208 ITR (St.) 32 also indicates that the legislative change was brought about to overcome the judicial interpretation of section 55(2)(a) dealing with the cost of acquisition. That circular does not refer to capital gains under section 56 as is sought to be contended. The circular clearly shows that the Income-Tax Act defines income to include capital gains chargeable under section 45. That, the judicial interpretation clearly laid down that only if an asset did cost something to the assessee in terms of money that the provisions relating to levy of tax under section 45 read with section 48 would apply. It is for this reason that the Finance Bill proposed to amend the provisions relating to capital gains and provide that the cost of acquisition of the tenancy rights be taken at nil. In the case of CIT v. Merchandisers (P.) Ltd., [1990] 182 ITR 107, the Division Bench of the Kerala High Court has considered the entire case law covering all judgments cited before us and has come to the

conclusion that no tax on capital gains could be levied in respect of transfer of the tenancy right. The Kerala High Court agreed with the view of the Delhi High Court in the case of Bawa Shiv Charan Singh v. CIT, [1984] 149 ITR 29 in which it has been held that if the computation provisions cannot apply to a given case then such a case could not be intended by the Legislature to fall within the charging section. That, if the whole of the value of the capital asset transferred is brought to tax, then, what would be charged is the capital value of the asset and not any profit and gain as contemplated in section 45. We agree with the view expressed by the Division Bench of the Kerala High Court in the case of Merchandisers (P.) Ltd, 's case, [1990] 182 ITR 107. Applying the ratio of the judgment of the Kerala High Court in the above case, we reject the contention of the Department that receipt of the surrender value on relinquishing of tenancy rights for consideration would constitute capital gains chargeable under section 56. As stated above, the Department has argued before us that since the asset surrendered had no cost of acquisition the capital gains arising on transfer of such an asset would fall under section 56. We do not find merit in this argument. A cost to the assessee in the acquisition of the asses is contemplated. If the whole of the value of the capital asset transferred is brought to tax under section 56 then what would be charged is the capital value of the asset and not any profit and gain as is contemplated

only in section 45. The term "capital asset" means property of any kind held by an assessee whether or not connected with his business or profession [see section 2(14)]. On the other hand, "capital gains" means any profit or gain arising from the transfer of a capital asset. Under section 2(47), the word "transfer" in relation to a capital asset is defined to include sale, exchange or relinquishment of the asset or extinguishment of any rights therein. In the present matter, the Department has not disputed that tenancy right is a property. It has not disputed that tenancy right is a capital asset. It has not disputed that surrender of the tenancy rights constituted transfer. Section 48 provides that from the full value of consideration received or accruing as a result of the transfer of capital asset, the following amounts should be deducted to arrive at capital gains, viz., cost of acquisition; expenditure on improvement; expenditure wholly and exclusively connected with transfer of the capital asset, such as stamp duty, registration charges, legal fees, brokerage, etc. Therefore, capital gains basically constitutes computation. According to the Department, the entire value of the capital asset transferred is taxable as the cost of acquisition in the case of tenancy cannot be ascertained. We do not find any merit in this argument. If the full value of the consideration received as a result of the transfer of tenancy is made taxable, then the tax is not levied on the capital gains, but, in substance, it is being levied on the capital value of the

asset. This is not permissible under section 56. The full consideration minus the cost of acquisition results in capital gains. However, the Department seeks to tax the full consideration on the ground that cost of acquisition is not ascertainable. If this contention is accepted, then the tax is not levied on capital gains, but it is being levied on the capital value of the asset which is not permissible under section 56 of the Act. This is also the ratio of the judgment of the Kerala High Court in the case of Merchandisers (P.) Ltd., [1990] 182 ITR 107. Hence, the above argument is rejected.

12. The intent of levying capital gains tax goes to the nature and character of the asset. It is an asset which possesses the inherent quality of being available on expenditure of money to a person seeking to acquire it. The courts have repeatedly held that none of the provisions pertaining to the head "Capital gains" suggests that "capital assets" include an asset in the acquisition of which no cost at all can be conceived. This is the clear ratio of the judgment of the Supreme Court in the case of B.C. Srinivasa Setty, [1981] 128 ITR 294. As long as the judgment of the Supreme Court in Anand Nivas's'case, AIR 1965 SC 414, held the field, the statutory tenancy remained a personal right. However, later on, in view of the judgment of the Supreme Court in the case of Kalyanji Gangadhar Bhagat v. Virji Bharmal, (1995) 3 SCC 725, tenancy rights clearly constitute capital assets. Under section 2(14) of the Income-Tax Act, capital asset has been

defined to mean property of any kind held by an assessee. Hence, tenancy right is a property. It falls under section 2(14) of the Income-Tax Act. As stated above, both sides have agreed on the footing that tenancy right is a property right. Both sides have argued on the footing that it is a capital asset. The only difference in the arguments of two sides is that, according to the Department, the Income-Tax Act seeks to tax capital gains arising from transfer of an asset which has no cost of acquisition under section 56 of, the Act (see the written propositions). As stated above, we do not find any merit in the above arguments. Even section 14 can only apply provided the receipt accrues on revenue account, either in the general sense or under the extended meaning given under the Income-Tax Act. Even if the Department seeks to bring such receipts under the residuary head, the onus is on the Department in the first instance to show as to how such a receipt would constitute income item. The Department has failed to discharge this burden. In the case of CIT v. J.V. Kolte, [1999] 235 ITR 239 (Bom), the Division Bench of this court laid down that in construing fiscal statutes and in determining the liability of a subject to tax, one must have regard to the strict letter of the law. That, the onus was on the Revenue to satisfy the court that, the case falls within the provisions of the law. That, if the case is not covered within the four corners of the provisions of the taxing statute, no tax can be imposed by inference or by analogy. That, if

a section in a taxing statute is of doubtful and ambiguous meaning, it is not possible to extract out of that ambiguity a new obligation not formerly cast upon the taxpayer. The observations of the above judgment applies to the facts of the present case. In the case of Withers v. Nethersole, [1948] 1 All ER 400, the House of Lords held that in cases involving sale of property with a limited life by a person not engaged in trade or profession of dealing in such property, the proceeds of such a sale were in the nature of capital and, therefore, not taxable. The Department, in that matter, came to the conclusion that the taxpayer was assessable to Income-Tax in respect of her share in the proceeds of the assignment of the exclusive motion picture rights in the novel and the play. It was not disputed before the House of Lords that the matter concerned assignment of the proprietary rights. The taxpayer under the relevant agreement made partial assignment of her copy right and she ceased to be the owner of that portion which was assigned for which she received a sum of money in exchange. The court held that this amounts to sale of property by a person, who was not engaged in the trade of dealing in such property. Therefore, the amount received by the taxpayer was a capital receipt. It was untaxable and not in the nature of taxable revenue. If the argument of the. Department is accepted, it would mean that all receipts would become taxable. It is well-settled that all receipts

are not taxable. Hence, we find merit in the case of the assessee.

13. It is essential also to bear in mind that income which falls-under one specified head could not be brought to tax under any other head. In the present matter, the Department did apply section 45. They did apply the head, viz., "Capital gains". However, when it came to computation, the Department found that cost of acquisition cannot be computed. Hence, it is now sought to be argued that such capital gains would constitute "income from other sources" under section 56. In the case of United Commercial Bank Ltd. v. CIT, [1957] 32 ITR 688 (SC), it has been held that income which falls under one specific head could not be brought to tax under any other head. If for any reason, the computation machinery fails, it is not open to the Department to apply the residuary clause."

(v) It is also relevant to state that in the instant case, the cost of acquisition of stock auctions by the petitioner cannot be determined and therefore, Section 48 of the I.T.Act cannot be applied; similarly, Section 45 is not applicable because the charging section and the computation section constitute an integrated code as held by the Apex Court in ***Mathuram Agarwal's case supra,*** as under:-

"*12. Another question that arises for consideration in this connection is whether sub-section (1) of Section 127-A and the proviso to sub-section (2)(b) should be construed together and the annual letting values of all the buildings owned by a person to be taken together for determining the amount to be paid as tax in respect of each building. In our considered view this position cannot be accepted. The intention of the legislature in a taxation statute is to be gathered from the language of the provisions particularly where the language is plain and unambiguous. In a taxing Act it is not possible to assume any intention or governing purpose of the statute more than what is stated in the plain language. It is not the economic results sought to be obtained by making the provision which is relevant in interpreting a fiscal statute. Equally impermissible is an interpretation which does not follow from the plain, unambiguous language of the statute. Words cannot be added to or substituted so as to give a meaning to the statute which will serve the spirit and intention of the legislature. The statute should clearly and unambiguously convey the three components of the tax law i.e. the subject of the tax, the person who is liable to pay the tax and the rate at which the tax is to be paid. If there is any ambiguity regarding any of these ingredients in a taxation statute then there is no tax in law. Then it is for the legislature to do the needful in the matter.*"

(vi) The material on record discloses that FSOPs are a right but not an obligation to buy the underlying instrument and represent a right to subscribe to the shares of a Company. On vesting, the option holder acquires an unfettered right to exercise the option and get the allotment of shares. The FSOPs have not been exercised yet and there are no shares in existence which have been allotted or transferred. A voluntary one-time payment of this nature before the allotment of shares cannot be taxed as perquisites. The stage from allotment of Stock Options to the sale of allotted shares is as follows:

a. Issuance of Stock Options
b. Vesting of Stock Options
c. Exercise of Stock Options
d. Issuance of shares
e. Sale of shares

Out of all the stages explained above, ESOPs are taxable at two instances. Firstly, where an employee exercises his option, then the difference between the fair market value and the exercise price is taxable as perquisite under Section 17(2)(vi) of the I.T.Act. Secondly, when the shares so allotted or transferred are sold by the employee, it is taxable as 'capital gains' under Section 45 of the I.T. Act.

In the present case, only the vesting of FSOPs has taken place to the petitioner. At this stage, there is no question of any income being computed on the FSOPs under the provisions of the Act. In any case, a one-time voluntary payment made by FPS without any corresponding contractual obligation and where a number of FSOPs admittedly remains the same does not constitute a revenue receipt that can be subject to Income Tax.

(vii) As rightly contended by the learned Senior counsel for the petitioner, the issue in controversy in relation to the subject FSOPs issued in favour of an employee of FIPL who was identically / similarly situated to that of the petitioner came up for consideration before the Division Bench of the Delhi High Court in ***Sanjay Baweja's case supra***, wherein it was held as under:-

> *The petitioner, vide the instant petition, seeks to assail the order dated 15.07.2023 passed under Section 197 of the Income Tax Act, 1961 ["Act"], whereby, the Revenue rejected the petitioner's application seeking 'Nil' deduction at source certificate.*
>
> *2. The brief facts relevant to appreciate the controversy at hand would reveal that the petitioner is an ex-employee of the company namely Flipkart Internet Private Limited ["FIPL"] which is a wholly-owned subsidiary of Flipkart Marketplace Private Limited ["FMPL"]. In addition thereto,*

the FMPL is the wholly-owned subsidiary of Flipkart Pvt. Ltd., Singapore ["FPS"].

3. In 2012, the FPS rolled out an Employee Stock Option Plan ["ESOP"] called as Flipkart Stock Option Plan ["FSOP"], wherein, the FPS granted certain stock options to the eligible persons, including employees of its subsidiaries. As per the clauses of FSOP, the petitioner was granted 1,27,552 stock options on and from 01.11.2014 to 31.11.2016 with a vesting schedule of 4 years.

4. On 23.12.2022, FPS announced the disinvestment of its wholly-owned subsidiary called PhonePe. Thereafter, the value of the stock options of FPS fell pursuant to the disinvestment and subsequent remittances to the shareholders of FPS on account of dividend payments, buy-back etc.

5. Consequently, on 21.04.2023, the petitioner received a communication from FPS stating that as a one-time measure, FPS had decided to grant the option holders a payment of USD 43.67 per option as compensation towards loss in the value of the options and it was based on the number of options held by the petitioner as on 23.12.2022. Furthermore, it was also stated that the FPS would be withholding tax on the said compensation.

6. Subsequently, on 29.04.2023, the petitioner preferred an application under Section 197 of the Act seeking a 'Nil' declaration certificate on the deduction of TDS by FPS. On

23.05.2023, the petitioner preferred a revised application under Section 197 of the Act.

7. Thereafter, on 15.07.2023, the Revenue passed the impugned order rejecting the petitioner's application on the score that the amount received would be in the nature of perquisite under Section 17(2)(vi) of the Act.

8. Aggrieved thereby, the petitioner has invoked the writ jurisdiction of this Court to ventilate his grievance.

9. Mr. Tarun Gulati, learned Senior Counsel, appearing on behalf of the petitioner submitted that the Revenue has misconstrued the onetime payment made on behalf of FPS as perquisite and characterized it as income chargeable to tax under Section 17(2)(vi) of the Act. He argued that ESOPs merely constitute a right, not an obligation to buy the underlying instrument and represent a right to subscribe to the shares of a company. He contended that on vesting, the option holder had acquired an unfettered right to exercise the option and got allotment of shares. He argued that ESOPs are taxable only in two contingencies- firstly, when the employee exercises his option and secondly, when the shares are sold by an employee. He iterated that in the present case, the stock options were merely held by the petitioner and the same had not been exercised till date.

10. Furthermore, he argued that the one-time voluntary payment made by FPS was not in relation to the employment of the petitioner with FIPL and thus, cannot partake the character of salary which was liable to be taxed

under Section 15 of the Act. It is, therefore, submitted that since the payment made by FPS cannot be construed as perquisite, the direction for deduction of TDS cannot be countenanced in law. In order to substantiate his submissions, he placed reliance on the decisions of Empire Jute Co. Ltd. v. CIT [1980] 3 Taxman 69/124 ITR 1/ 4 SCC 25, Shrimant Padmaraje R. Kadambande v. CIT [1992] 3 SCC 432., Godrej & Co. v. CIT 1959 SCC OnLine SC 101 and Empire Jute Co. Ltd.'s case (supra).

11. Per contra, Mr. Prashant Meherchandani, learned Senior Standing Counsel appearing on behalf of the Revenue, vehemently opposed the submissions. He argued that the present writ petition has become infructuous as the transaction already took place on 31.07.2023. He submitted that proceedings under Section 197 of the Act are not a fact-intensive exercise and rather, it is an administrative exercise and therefore, the AO was not obligated to dive into the matter to determine whether the stock option was exercised with the petitioner or not. He further argued that all the relevant facts pertaining to the FSOP were not produced before the authority earlier. In order to substantiate his arguments, he placed reliance on the decision of this Court in National Petroleum Construction Co. v. Dy. CIT 2019 SCC OnLine Del 12353 .

12. We have heard the learned counsels appearing on behalf of the parties and perused the record.

13. The short controversy that emerges for resolution in the present case is whether the one-time payment made on

behalf of FPS formed a part of salary under Section 17 of the Act or not? The consequential question of taxability of such payment is contingent upon the aforesaid issue and shall be answered as a corollary of the same.

14. For the sake of convenience, the relevant extracts of the order impugned before us are reproduced herein for reference:-

"After perusal of the facts of the case and the written submissions of the Assessee, following observations are made.

1. The assessee has contended that the amount receivable by him for FPS does not constitute income u/s 2 (24) of the Income Tax Act, 1961. In this regard, it is observed that section 2 (24) of the Act provides an inclusive definition of "Income" and it is not an exhaustive definition. Thus even if a nature of receipt is not specifically mentioned under this section, it may still be includible in the taxable income of the assessee, depending upon the facts of the case.

1. General rule is that every amount received by an assessee is taxable unless it is specifically exempt under any provisions of the Act. The assessee has contended that this receipt is not taxable but he has failed to quote any express provisions of the Income Tax Act under which this receipt would be exempt from tax.

1. The assessee has himself stated that M/s FPS intends to withhold full tax on the said payment, which is why he

has applied for issuance of a Nil TDS certificate. If the amount receivable by the assessee is not an "income" and not taxable under the Income Tax Act, then why the payer intends to withhold tax on the same. It implies that the payer is satisfied that the payment being made by it is subject to withholding tax. Thus the assessee should have contended before the payer company that this payment would not be subject to withholding tax but interestingly, the assessee has not challenged the deduction of tax at source by the payer but instead he has chosen to request for issuance of a Nil TDS certificate.

1. The assessee has not been able to satisfactorily prove that the amount receivable by him would be exempt under any express provisions of the Act.

1. The assessee has stated that he would be reporting this income as exempt in his ITR. Since the quantum of income sought to claimed as exempt is quite substantial, there is a high probability that this ITR would selected for scrutiny assessment and if the claim of the assessee is not accepted by the assessing officer, it may result in creation of tax demand. Hence issuance of a Nil TDS certificate at this stage would be detrimental to the interest of revenue and recovery of taxes.

1. Section 17 (2) (vi) of the Act states that Perquisite includes

"...the value of any specified security or sweat equity shares allotted or transferred, directly or indirectly, by the employer or former employer , free of cost or at

concessional rate to the assessee.." The phrase "directly or indirectly" used in the above clause implies that the amount receivable by the assesse in the instant case would be covered under the purview of "Perquisite", which is included in the salary as per section 17 (1) (iv) of the Act.

Compensation payable for the diminution of the intrinsic value of ESOPs held by an employee including an ex-employee would be in the nature of income, and the same is not specifically exempt under the Act.

The compensation is linked to the vested ESOPs in the instant case. ESOPs result in a taxable perquisite on the allotment of shares equivalent to the fair market value less the exercise price of the shares so allotted under section 17(2)(vi) and is taxable under the head 'Salaries' in hands of the employee or ex-employee, as the case may be. Consequently, the compensation receivable on the said ESOPs, even though from a former employer, directly or indirectly, on account of diminution of fair value of the underlying shares, should also have the same characterization and tax treatment and hence, in my view, is taxable under the head 'Salaries'. It also does not matter whether the said amount is being paid by the former employer directly to the assessee or through any of its group companies indirectly and the amounts would remain taxable as salary. Further, this amount would have been taxable as salary if the assessee would have been in current employment with the payer or its group companies and hence, the amounts would remain taxable as salary

even if the assessee is no longer employed with the payer or its group companies. Having come to the conclusion that the compensation should be chargeable to tax under the head 'Salaries', provisions of section 192 of the Act would apply and accordingly, the employer is under an obligation to deduct tax while making the payment of the compensation to the Assessee. The taxability under the other heads of income is not relevant since the same is taxable under the head 'Salaries'.

In view of the above discussion, it is proposed that, if approved, the application of the Assessee for issuance of a Nil TDS certificate may be rejected."

15. A bare perusal of the impugned order would reveal that the Revenue characterized the one-time payment made by FPS to the petitioner under the head of a perquisite, as defined in Section 17(2)(vi) of the Act, on the ground that the payment received was linked to ESOPs as a form of compensation for diminution of the fair market value of stocks.

16. At the outset, it is relevant to point out that this Court vide order dated 23.08.2023 directed the petitioner to file an affidavit apprising about the number of options held by him as on the record date. Pursuant to the said order, the petitioner filed an affidavit stating that out of the total number of shares i.e., 1,27,552 allotted to him, he holds 33,482 stock options as on the record date of 23.12.2022. The detailed calculation as appended in the tabular chart is reproduced herein for reference:-

S No.	Particulars	No. of stock options/compensation
i.	Options granted	1,27,552
ii.	Vested options (25% of the total options granted) after 1 year i.e.01.11.2015	[25% of (*i*)] =31,888
iii.	Remaining 75% stock options to be vested in next 36 months	[(*i*)-(*ii*)] =95,664 95,664/36=(2657/ month)
iv.	Vested Options upto 31.10.2016	(2657x12 months) =31,884
v.	Total vested options upto 31.10.2016	[(*i*)+(*v*)] =63,772
vi.	Cancelled options on account of termination of employment on 31.10.2016	[(*i*)-(*v*)] =63,780
vii.	Options repurchased by Walmart in the year 2017 (25% of the total vested stock options)	[25% of (*v*)] =15943
viii.	Remaining vested stock options after repurchase by walmart	[(*v*)-(*vi*)] =47,829
ix.	Options repurchased by Walmart in the year 2018 (30% of the total remaining vested stock options)	[30% of (*viii*)] =14,347
x.	Balance as on record date	[(*viii*)-(*ix*)] =33482
xi.	Compensation	[(*x*) x Compensation per stock options x USD conversion rate] 33,482 x 43.67 x 82 =Rs. 11,98,97,033/-

17. As the facts of the matter suggest, undisputedly, the petitioner has not exercised his vested right with respect to stock option under FSOP till date, which signifies that the right of holding the stocks under his name had not been exercised. Therefore, the moot question is only limited to the extent whether the one-time voluntary payment made on behalf of FPS to the petitioner can be pegged as perquisite under Section 17(2)(vi) of the Act.

18. It is germane to point out that the perquisites, as defined in Section 17(2) of the Act, constitute a list of benefits or advantages, which are made taxable and are incidental to employment and received in excess of salary. Furthermore, as per Section 17(2)(vi) of the Act, perquisite refers to value of any specified security or sweat equity shares allotted or transferred, directly or indirectly, by the employer, or former employer, free of cost or at concessional rate to the petitioner. The explanation appended to Section 17(2)(vi) of the Act also clarifies that the value of any specified security shall be the difference in the amount of fair market value of the specified security on the date on which the option was exercised and the actual amount paid by the petitioner. For the sake of convenience, Section 17(2)(vi) of the Act and the explanation thereto is reproduced herein for reference:-

17. "Salary", "perquisite" and "profits in lieu of salary" defined.—For the purposes of Sections 15 and 16 and of this section.—

*****

(2) "Perquisite" includes—

*****

[(vi) the value of any specified security or sweat equity shares allotted or transferred, directly or indirectly, by the employer, or former employer, free of cost or at concessional rate to the assessee.

Explanation.— For the purposes of this sub-clause,—

(a) "specified security" means the securities as defined in clause (h) of Section 2 of the Securities Contracts (Regulation) Act, 1956 (42 of 1956) and, where employees' stock option has been granted under any plan or scheme therefor, includes the securities offered under such plan or scheme;

(b) "sweat equity shares" means equity shares issued by a company to its employees or directors at a discount or for consideration other than cash for providing know-how or making available rights in the nature of intellectual property rights or value additions, by whatever name called;

(c) the value of any specified security or sweat equity shares shall be the fair market value of the specified security or sweat equity shares, as the case may be, on the date on which the option is exercised by the assessee as reduced by the amount actually paid by, or recovered from the assessee in respect of such security or shares;

(d) "fair market value" means the value determined in accordance with the method as may be prescribed;

(e) "option" means a right but not an obligation granted to an employee to apply for the specified security or sweat equity shares at a predetermined price"

19. At this juncture, it is imperative to point out that the determination as to whether a particular receipt would tantamount to a capital receipt or revenue receipt is dependent upon the factual scenario of a particular case. This position was also fructified in the decision

of CIT v. Saurashtra Cement Ltd. [2010] 192 Taxman 300/325 ITR 422/ 11 SCC 84. The relevant paragraphs of the said decision are reproduced herein for reference:-

"14. The question whether a particular receipt is capital or revenue has frequently engaged the attention of the courts but it has not been possible to lay down any single criterion as decisive in the determination of the question. Time and again, it has been reiterated that answer to the question must ultimately depend on the facts of a particular case, and the authorities bearing on the question are valuable only as indicating the matters that have to be taken into account in reaching a conclusion.

15. In Rai Bahadur Jairam Valji [AIR 1959 SC 291 : (1959) 35 ITR 148] it was observed thus: (AIR pp. 292-93, para 2)

"2. The question whether a receipt is capital or income has frequently come up for determination before the courts. Various rules have been enunciated as furnishing a key to the solution of the question, but as often observed by the highest authorities, it is not possible to lay down any single test as infallible or any single criterion as decisive in the determination of the question, which must ultimately depend on the facts of the particular case, and the authorities bearing on the question are valuable only as indicating the matters that have to be taken into account in reaching a decision. [Vide Van Den Berghs Ltd. (Inspector of Taxes) v. Clark [1935 AC 431 : (1935) 3 ITR (Eng Cas) 17 (HL)] .] That, however, is not to say that the question is

one of fact, for, as observed in Davies (Inspector of Taxes) v. Shell Co. of China Ltd. [(1951) 32 TC 133 : (1952) 22 ITR Supp 1 (CA)] :

'these questions between capital and income, trading profit or no trading profit, are questions which, though they may depend no doubt to a very great extent on the particular facts of each case, do involve a conclusion of law to be drawn from those facts.' "

16. In Kettlewell Bullen and Co. Ltd. [AIR 1965 SC 65] dealing with the question whether compensation received by an agent for premature determination of the contract of agency is a capital or a revenue receipt, echoing the views expressed in Rai Bahadur Jairam Valji [AIR 1959 SC 291 : (1959) 35 ITR 148] and analysing numerous judgments on the point, this Court laid down the following broad principle, which may be taken into account in reaching a decision on the issue: (Kettlewell Bullen and Co. Ltd. case [AIR 1965 SC 65] , AIR p. 79, para 36)

"36. ... Where on a consideration of the circumstances, payment is made to compensate a person for cancellation of a contract which does not affect the trading structure of his business, nor deprive him of what in substance is his source of income, termination of the contract being a normal incident of the business, and such cancellation leaves him free to carry on his trade (freed from the contract terminated) the receipt is revenue: where by the cancellation of an agency the trading structure of the assessee is impaired, or such cancellation results in loss

of what may be regarded as the source of the assessee's income, the payment made to compensate for cancellation of the agency agreement is normally a capital receipt."

20. As per the understanding of the Revenue, the said one-time voluntary payment at the discretion of the management of FPS shall be pegged under the head of perquisite as per Section 17(2)(vi) of the Act. It is thus pertinent to point out the observations made by the Supreme Court in the case of Shrimant Padmaraje R. Kadambande (supra), wherein one-time voluntary cash allowance was given to the assessee and the Court held that such monetary receipts, rather it was a capital receipt and thus, not liable to tax. The relevant paragraphs of the said decision are reproduced as under:-

"15. A case similar to the one on hand is H.H. Maharani Shri Vijaykuverba Saheb of Morvi [[1963] 49 ITR 594 (Bombay)] wherein the High Court held that a voluntary payment without consideration cannot fall in the category of income. The position here is exactly the same. There is no compulsion on the part of the Government to give any allowance. It is purely discretionary. It cannot be got over by saying that after the order is passed the assessee gets a right. That has nothing to do in determining the question.

16. In S.R.Y. Sivaram Prasad Bahadur [(1971) 3 SCC 726, 732 : (1971) 82 ITR 527, 535] in no uncertain terms it was laid down that it is the quality of the payment that is decisive of the character of the payment and not the method of payment or its measure which will make it fall

within the category of capital or revenue. Undoubtedly, the High Court had not kept these important aspects before rendering the decision whether it is a revenue receipt or not. The judgment of the High Court requires to be interfered with.

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27. Therefore, in this case, the maintenance allowance was qualified by the statute and it was a nomenclature peculiarly suited to payments of the nature of income. The learned counsel for the Revenue would state if the payments in this case do not constitute windfall and the right to payment of these cash allowances in the case on hand, could be enforced in a civil court, as laid down in this ruling, there is no other way than to hold this to be an income. But, as we have pointed out just now, maintenance allowance is qualified by statute unlike the present case which is purely a discretionary payment. It is no use contending as also observed by the High Court that after the order is passed an enforceable right arises. On the contrary the question would be whether the statute gives an enforceable right. We think, in such of those cases falling under clause (d) of the proviso to Section 15(1) of the Act, no statutory right is created. This is unlike those cases falling under clauses (i), (ii) and (iii) of sub-section (1) of Section 15. These constitute different clauses as has already been pointed out by us. The fact that the assessee has applied for a grant for maintenance,

nor again, the periodicity of payment, would be conclusive as we will demonstrate later.

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35. There is no compulsion on the part of the Government to make the payment nor is the Government obliged to make the payment since it is purely discretionary. A case similar to the one on hand is H.H. Maharani Shri Vijaykuverba Saheb of Morvi [[1963] 49 ITR 594 (Bombay)] head-note of which is extracted:

"A voluntary payment which is made entirely without consideration and is not traceable to any source which a practical man may regard as a real source of his income but depends entirely on the whim of the donor cannot fall in the category of income.

The ruler of a native State abdicated in favour of his son in January, 1948. From April, 1949, onwards his son paid him a monthly allowance. The allowance was not paid under any custom or usage. The allowance could not be regarded as maintenance allowance, as the assessee possessed a large fortune.

Held, that as the payments were commenced long after the ruler had abdicated, they were not made under a legal or contractual obligation. As the allowances were not also made under a custom or usage or as a maintenance allowance, they were not assessable."

36. The position is exactly the same. The payment made by the Government is undoubtedly voluntary. However, it

has no origin in what might be called the real source of income. No doubt Section 15(1) proviso clause (d) enables the applicant to seek payment but that is far from saying that it is a source. Therefore, it cannot afford any foundation for such a source. Further, it is a compassionate payment, for such length of period as the Government may, in its discretion, order.

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39. As a result of the above discussion, we hold that the amounts received by the assessee during the financial years in question have to be regarded as capital receipts and, therefore, are not income within the meaning of Section 2(24) of the Income Tax Act. Accordingly, we set aside the judgment of the High Court and allow the appeals with no order as to costs."

21. It is also significant to place reliance on the decision of the Supreme Court in the case of Godrej & Co. (supra), wherein, one-time payment was given to an assessee company in lieu of a change in contractual terms between the assessee company and the management company. In the light of such facts, such monetary receipts were also clubbed under the head of capital receipt and not under the revenue receipts and thus, not liable to tax. The relevant paragraph no. 8 of the said decision is reproduced herein for reference:-

"8. This sum of Rs 7,50,000 has undoubtedly not been paid as compensation for the termination or cancellation of an ordinary business contract which is a part of the stock-

in-trade of the assessee and cannot, therefore, be regarded as income, as the amounts received by the assessee in CIT and Excess Profits Tax v. South India Pictures Ltd [(1956) SCR 223, 228] and in CIT v. Rai Bahadur Jairam Valji [(1959) 35 ITR 148 : (1959) SCR Supp 110] had been held to be. Nor can this amount be said to have been paid as compensation for the cancellation or cessation of the managing agency of the assessee firm, for the managing agency continued and, therefore, the decision of the Judicial Committee of the Privy Council in CIT v. Shaw Wallace and Co. [(1932) LR 59 IA 206] cannot be invoked. It is, however, urged that for the purpose of rendering the sum paid as compensation to be regarded as a capital receipt, it is not necessary that the entire managing agency should be acquired. If the amount was paid as the price for the sterilisation of even a part of a capital asset which is the framework or entire structure of the assessee's profit making apparatus, then the amount must also be regarded as a capital receipt, for, as said by Lord Wrenbury in Glenboig Union Fireclay Co. Ltd. v. IRC [(1922) 12 TC 427] "what is true of the whole must be equally true of part"— a principle which has been adopted by this Court in CIT v. Vazir Sultan and Sons [Civil Appeal No. 346 of 1957, decided on March 20, 1959;(1959) 36 ITR 175] . The learned Attorney-General, however, contends that this case is not governed by the decisions in Shaw Wallace's case [(1932) LR 59 IA 206] or Vazir Sultan and Son case [Civil Appeal No. 346 of 1957, decided on March 20, 1959;(1959) 36 ITR 175] because in

the present case there was no acquisition of the entire managing agency business or sterilisation of any part of the capital asset and the business structure or the profit making apparatus, namely, the managing agency, remains unaffected. There is no destruction or sterilisation of any part of the business structure. The amount in question was paid in consideration of the assessee firm agreeing to continue to serve as the managing agent on a reduced remuneration and, therefore, it bears the same character as that of remuneration and, therefore, a revenue receipt. We do not accept this contention. If this argument were correct, then, on a parity of reasoning, our decision in Vazir Sultan and Sons case [Civil Appeal No. 346 of 1957, decided on March 20, 1959;(1959) 36 ITR 175] would have been different, for, there also the agency continued as before except that the territories were reduced to their original extent. In that case also the agent agreed to continue to serve with the extent of his field of activity limited to the State of Hyderabad only. To regard such an agreement as a mere variation in the terms of remuneration is only to take a superficial view of the matter and to ignore the effect of such variation on what has been called the profit-making apparatus. A managing agency yielding a remuneration calculated at the rate of 20 per cent of the profits is not the same thing as a managing agency yielding a remuneration calculated at 10 per cent of the profits. There is a distinct deterioration in the character and quality of the managing agency viewed as a profit-making apparatus and this deterioration is of an

enduring kind. The reduced remuneration having been separately provided, the sum of Rs 7,50,000 must be regarded as having been paid as compensation for this injury to or deterioration of the managing agency just as the amounts paid in Glenboig case [(1922) 12 TC 427] or Vazir Sultan case [Civil Appeal No. 346 of 1957, decided on March 20, 1959;(1959) 36 ITR 175] were held to be. This is also very nearly covered by the majority decision of the English House of Lords in Hunter v. Dewhurst [(1932) 16 TC 605] . It is true that in the later English cases of Prendergast v. Cameron [(1940) 23 TC 122] and Wales Tilley [(1943) 25 TC 136] the decision in Hunter v. Dewharst [(1932) 16 TC 605] was distinguished as being of an exceptional and special nature but those later decisions turned on the words used in Rule 1 of Schedule E. to the English Act. Further, they were cases of continuation of personal service on reduced remuneration simpliciter and not of acquisition, wholly or in part, of any managing agency viewed as a profit-making apparatus and consequently the effect of the agreements in question under which the payment was made upon the profit making apparatus, did not come under consideration at all. On a construction of the agreements it was held that the payments made were simply remuneration paid in advance representing the difference between the higher rate of remuneration and the reduced remuneration and as such a revenue receipt. The question of the character of the payment made for compensation for the acquisition, wholly or in part, of any managing agency or injury to or

deterioration of the managing agency as a profit-making apparatus is covered by our decisions hereinbefore referred to. In the light of those decisions the sum of Rs 7,50,000 was paid and received not to make up the difference between the higher remuneration and the reduced remuneration but was in reality paid and received as compensation for releasing the company from the onerous terms as to remuneration as it was in terms expressed to be. In other words, so far as the managed company was concerned, it was paid for securing immunity from the liability to pay higher remuneration to the assessee firm for the rest of the term of the managing agency and, therefore, a capital expenditure and so far as the assessee firm was concerned, it was received as compensation for the deterioration or injury to the managing agency by reason of the release of its rights to get higher remuneration and, therefore, a capital receipt within the decisions of this Court in the earlier cases referred to above."

22. It is also apposite to deal with the contention of the Revenue that the facts pertaining to the exercise of the options held by the petitioner were not apprised to the AO in the proceedings referrable to Section 197 of the Act. On the said aspect, it was contended that in such a scenario, only the facts which were before the AO should be kept in mind while deciding the present controversy. However, a bare perusal of the application dated 29.04.2023 made by the petitioner under Section 197 of the Act, which has been appended in the petition as Annexure-P4, would

reveal that the petitioner had duly placed the pertinent details alluding to FSOP.

23. Furthermore, the record available before us would reflect that the AO had never enquired or asked for clarification from the petitioner regarding any other significant details pertaining to FSOP. In addition thereto, the reliance placed by the Revenue in the case of National Petroleum Construction Co. (supra) is also misplaced as in that case, the issue pertained to the determination of permanent establishment in Section 197 proceedings. However, in the present case, the relevant facts pertaining to the ESOP and details alluding to one-time voluntary payment made by FPS to the petitioner were placed on the desk of the concerned AO, while making an application under Section 197 of the Act.

24. Interestingly, the reasoning appended in the impugned order also hinges upon the fact that since FPS intended to deduct tax before making the payment, therefore, the amount was liable to be taxed. It is pertinent to note that the manner or nature of payment, as comprehensible by the deductor, would not determine the taxability of such transaction. It is the quality of payment that determines its character and not the mode of payment. Unless the charging Section of the Act elucidates any monetary receipt as chargeable to tax, the Revenue cannot proceed to charge such receipt as revenue receipt and that too on the basis of the manner or nature of payment, as comprehensible by the deductor. Such a position was also

settled in the decision of the Supreme Court in the case of Empire Jute Co. Ltd. (supra), wherein, it was held as under:-

"4. Now an expenditure incurred by an assessee can qualify for deduction under Section 10(2)(xv) only if it is incurred wholly and exclusively for the purpose of his business, but even if it fulfils this requirement, it is not enough; it must further be of revenue as distinguished from capital nature. Here in the present case it was not contended on behalf of the Revenue that the sum of Rs 2,03,255 was not laid out wholly and exclusively for the purpose of the assessee's business but the only argument was and this argument found favour with the High Court, that it represented capital expenditure and was hence not deductible under Section 10(2)(xv). The sole question which therefore arises for determination in the appeal is whether the sum of Rs 2,03,255 paid by the assessee represented capital expenditure or revenue expenditure. We shall have to examine this question on principle but before we do so, we must refer to the decision of this Court in Maheshwari Devi Jute Mills case [AIR 1965 SC 1974 : (1965) 3 SCR 765 : (1965) 57 ITR 36] since that is the decision which weighed heavily with the High Court, in fact, compelled it to negative the claim of the assessee and hold the expenditure to be on capital account. That was a converse case where the question was whether an amount received by the assessee for sale of loom hours was in the nature of capital receipt or revenue receipt. The view taken by this Court was that it was in the nature of

capital receipt and hence not taxable. It was contended on behalf of the Revenue, relying on this decision, that just as the amount realised for sale of loom hours was held to be capital receipt, so also the amount paid for purchase of loom hours must be held to be of capital nature. But this argument suffers from a double fallacy.

5. In the first place it is not a universally true proposition that what may be capital receipt in the hands of the payee must necessarily be capital expenditure in relation to the payer. The fact that a certain payment constitutes income or capital receipt in the hands of the recipient is not material in determining whether the payment is revenue or capital disbursement qua the payer. It was felicitously pointed out by Macnaghten, J., in Racecourse Betting Control Board v. Wild [22 TC 182 : (1938) 4 All ER 487] that a "payment may be a revenue payment from the point of view of the payer and a capital payment from the point of view of the receiver and vice versa". Therefore, the decision in Maheshwari Devi Jute Mills case [AIR 1965 SC 1974 : (1965) 3 SCR 765 : (1965) 57 ITR 36] cannot be regarded as an authority for the proposition that payment made by an assessee for purchase of loom hours would be capital expenditure. Whether it is capital expenditure or revenue expenditure would have to be determined having regard to the nature of the transaction and other relevant factors."

[Emphasis supplied]

25. Pertinently, as per Section 17(2)(vi) of the Act, the perquisites include value of any specified security allotted or transferred, directly or indirectly, by the employer, or former employer, free of cost or at concessional rate to the petitioner. The most crucial ingredient of this inclusive definition is - determinable value of any specified security received by the employee by way of transfer/allotment, directly or indirectly, by the employer. As per Explanation (c) to Section 17(2)(vi) of the Act, the value of specified security could only be calculated once the option is exercised. A literal understanding of the provision would provide that the value of specified securities or sweat equity shares is dependent upon the exercise of option by the petitioner. Therefore, for an income to be included in the inclusive definition of "perquisite", it is essential that it is generated from the exercise of options, by the employee. The facts of the present case suggest that the petitioner has not exercised his options under the FSOP till date. Under the facts of the present case, the stock options were merely held by the petitioner and the same have not been exercised till date and thus, they do not constitute income chargeable to tax in the hands of the petitioner as none of the contingencies specified in Section 17(2)(vi) of the Act have occurred.

26. Moreover, the compensation was a voluntary payment and not transfer by way of any obligation. Notably, the present is not a case where the option holder has exercised his right. Rather, the facts suggest that the petitioner has not exercised his options under the FSOP till

date. It appears that due to the disinvestment of the PhonePe business from FPS, the Board of Directors of FPS had decided to provide a one-time voluntary payment to all the option holders pursuant to FSOP. It is imperative to point out that the management proceeded by noting that there was no legal or contractual right under FSOP to provide compensation for loss in current value or any potential losses on account of future accretion to the ESOP holders. It was further noted that FPS, on its own discretion, has estimated and decided to pay USD 43.67 as compensation for each stock option as held on the record date. The relevant extract of the said communication dated 21.04.2023 is reproduced herein for reference:-

"Dear All, As you are aware, the Board of Directors (BoD) of Flipkart Private Limited, publicly announced the complete separation of PhonePe business, by selling off its entire shareholding, in Dec 2022. With this announcement, the value of ESOPs granted to all stakeholders (including present and former employees in our subsidiaries in India, Israel, US, Singapore, Saudi Arabia, Egypt, UAE, China etc.) will drop, along with loss of opportunity to share in future accretion in the value of Phonepe shares. While there is no legal or contractual right under FSOP 2012, to provide compensation for loss in current value or any potential losses on account of future accretion to our ESOP holders, the BoD on its own discretion, has decided to pay US$43.67 as compensation for each ESOP subject to applicable withholding taxes and

other tax rules in respective countries of various ESOP holders".

27. Therefore, it is elementary to highlight that the payment in question was not linked to the employment or business of the petitioner, rather it was a one-time voluntary payment to all the option holders of FSOP, pursuant to the disinvestment of PhonePe business from FPS. In the present case, even though the right to exercise an option was available to the petitioner, the amount received by him did not arise out of any transfer of stock options by the employer. Rather, it was a onetime voluntary payment not arising out of any statutory or contractual obligation.

28. Thus, the reasoning appended to the impugned order, holding that the amount in question tantamount to perquisite under Section 17 (2)(vi) of the Act, cannot be countenanced in law, as the stock options were not exercised by the petitioner and the amount in question was onetime voluntary payment made by FPS to all option holders in lieu of disinvestment of PhonePe business.

29. Accordingly, we set aside the impugned order dated 15.07.2023. We, however, note that since the transaction already took place on 31.07.2023, we, accordingly, accord liberty to the petitioner to file an application for refund of TDS amount before the Revenue. It is further directed to the Revenue to consider the application of the petitioner in view of the observations made hereinabove and as per extant regulations.

> *30. In view of the aforesaid, the writ petition is allowed in the above terms and disposed of, along with pending applications, if any."*

As can be seen from the aforesaid judgment, the Delhi High Court while dealing in the exact facts and circumstance where the onetime payment made by FPS on account of diminution of value of stock option, pursuant to the divestment of PhonePe was held to be perquisites under Section 17(2)(vi) of the I.T.Act by the Revenue, the Court while quashing the impugned order passed under Section 197 of the Act held that:

a. Section 17(2)(vi) I.T.Act does not apply before the exercise of options and before the issuance of shares.

b. A onetime voluntary payment is a capital receipt and not a revenue receipt.

c. Merely because the deductor has sought to deduct TDS would not determine the taxability of a transaction.

d. The payment was not linked to the employment of the petitioner.

e. There was no transfer of any stock options by the petitioner.

f. The petitioner was entitled to apply for a refund of TDS as the amount received was not taxable in his hands.

The above judgment was rendered in the case of another Employee of Flipkart in the identical set of facts and the very same transaction, which is the subject matter of the present writ petition and the reasoning of the judgment squarely applies to the facts of the instant case of the petitioner.

(viii) The respondents have placed reliance upon the subsequent judgment of the learned Single Judge of the Madras High Court in ***Nishithkumar's case supra,*** in order to contend that the judgment of the Delhi High Court has been held to be incorrect and the application filed by the petitioner – assessee therein was dismissed by the Madras High Court; with due respect, I do not subscribe to the views of the learned Single Judge of the Madras High Court and I am in complete agreement with the judgment of the Division Bench of the Delhi High Court in ***Sanjay Baweja's case supra,*** for more than one reason;

(a) The judgment of the Delhi High Court was not challenged by the respondents – revenue and the same has attained finality and become conclusive and binding upon the revenue.

(b) The petitioner – assessee has challenged the judgment of the Madras High Court in ***Nishithkumar's case supra,*** by

preferring an appeal in W.A.No.198/2025 and the same is pending consideration, thereby indicating that the judgment of the learned Single Judge has still not attained finality.

(c) The order impugned before the learned Single Judge categorically held that the compensation could not be charged to perquisites under the Head 'salary' ; before the learned Single Judge of the Madras High Court, an order dated 12.07.2023 under Section 197 of the Act was impugned. The said order had come to a conclusive finding that "the compensation to be received is not chargeable under the head salaries", this finding was not in challenge by either the assessee or the Income Tax Department. A reading of the aforesaid Judgment also demonstrates that no argument either by the assessee or the department was made whether the compensation could be taxed as perquisites under the head 'salaries' or not. Despite, no issues having been raised by either side, the learned Single Judge erroneously come to a finding that compensation could be held as perquisites and charged to tax under the salary.

(d) It is relevant to state that the aforesaid order of the learned Single Judge has not been accepted by the assessee and

an appeal has been filed against the aforesaid order, which is pending consideration.

(e) The order impugned before the learned Single Judge was that the compensation could be taxed under the head Capital Gain because the assessee had transferred the right to sue which was a capital asset: the only issue involved before the learned Single Judge was whether the order impugned was correct in holding that there was a right to sue which was created in favor of the assessee and that such right to sue was a capital asset which was transferred by the assessee and the compensation received could be regarded as consideration for such a transfer and could be taxed under the head 'Capital Gain'. The learned Single Judge categorically came to the finding at that the impugned order was incorrect and the finding that the compensation was liable to be taxed under the Head ‘Capital Gain’ was incorrect and having said so, the learned Single Judge ought to have allowed the writ petition and set aside the order impugned before it.

(f) The finding that ESOPS are not capital asset is erroneous: It is seen that the learned Single Judge erroneously held that ESOPs are not capital asset and that the term 'Capital Asset' are defined under Section 2(14) of the Act as *"property of any kind held by an assessee, whether or not connected with his business or profession*". The definition is extremely wide and covers property of all kind which includes rights in assets.

(g) The learned Single Judge misconstrued the Explanation-I to Section 2(14) of the Act which merely explains that rights in or in relation to an Indian Company, such as rights of management or control and only share of an Indian company could be considered as Capital Assets. The learned Single Judge failed to appreciate that the said Explanation could not lead to a conclusion that rights in shares of a foreign company could not be regarded as "property of any kind" and therefore, be treated as capital asset. The findings are also contrary to the judgment of the Apex Court in ***Hari Brothers Private Limited vs. ITO - [1964] 54 ITR 399*** and ***Chitranjan A. Dasann Acharya vs. CIT-05 - [2020] 429 ITR 570***, which clearly held that any right which is relatable to share or subscription of shares is a capital asset.

(h) The incorrect finding that ESOPs are not in the nature of profit making structure or capable of revenue generation: the learned Single Judge erroneously held that ESOPs are not a source of revenue and not capable of generating revenue. In this regard, it is necessary to state that the options held by the petitioner are capital assets which are admittedly an income earning source and it is a settled principle of law that the compensation/windfall awarded in lieu of diminishing of profit making structure would be a 'capital receipt'.

(i) The judgments of the Apex Court on the issue of capital receipts relied upon by the Delhi High Court were incorrectly distinguished: The Delhi High Court had relied on several judgments of the Apex Court to hold that a onetime voluntary compensation for the diminution in value of profit making structure would amount to a capital receipt not chargeable to income tax. These judgments fully apply to the facts of the case where the divestment of PhonePe business by FPS would lead to a permanent loss and value of the ESOPs as the ability to generate profits from such business and would no longer enrich the value of ESOPs or the resultant shares. The learned Single Judge

erroneously held that such ESOPs would be actionable claim not capable of generating revenue and ignored the fact that there was a permanent loss of revenue generating source.

(j) The compensation has been erroneously held to be 'perquisites' by the learned Single Judge who erroneously concluded that the ESOP granted to the petitioner qualifies as ESOP under Companies Act, 2013 and consequently, fall within the scope of Explanation(a) to Section 17(2)(vi) of the I.T. Act. In this regard, it is seen that taxability of ESOPs is well settled, inasmuch as, when an employee exercises his vested option, then the difference between the fair market value and the exercise price is taxable as perquisite under Section 17(2)(vi) of the I.T. Act. Secondly, when the shares so allotted or transferred are sold by the employee, it is taxable as 'capital gains' under Section 45 of the I.T.Act. Further, in the instant case, the petitioner has not exercised its options till date and therefore, Section 17(2)(vi) of the I.T. Act cannot be invoked at all. In any case, in absence of a calculation mechanism receipts cannot be taxed as held by the Apex Court in ***CIT v. B.C.Srinivas Setty - 128 ITR 294 (SC),*** wherein, it was held that if the cost of acquisition cannot be ascertained, in that case,

capital gains cannot be attracted. The learned Single Judge ignored the well settled principle that in the absence of computational mechanism, no tax can be charged.

(k) The learned Single Judge rendered an erroneous finding by holding that ESOPs would come within the purview of the term "Specified Security. In this context, it is necessary to state that specified securities is defined in Explanation (a) to Section 17(2)(vi) of the I.T.Act, which clearly does not include ESOPs and only refers to stocks and other securities which are included as securities under Securities and Contract Regulation Act.

(l) The finding of the learned Single Judge that ESOPs can be regarded as specified security and the consequent finding that Section 17(2)(vi) of the I.T.Act is wide enough to include a discretionary compensation paid to ESOP holders and can be taxed as perquisites is incorrect. Firstly, the above finding is contradictory to the findings that ESOPs are not "property of any kind". Secondly, this finding loses sight of the fact that the computational mechanism provided for under Section 17(2)(vi) of the I.T.Act contemplates the following:

The existence of shares or other securities;

The ascertainment of fair market value of such shares on the date of allotment;

The deduction of the cost of such shares in the hands of the assessee to compute the perquisites.

None of the above ingredients were available when the compensation was received by the assessee and therefore, the tax was incapable of being computed.

(m) Compensation was not received by the employer or former employer thus, was not restricted to employees alone: The learned Single Judge lost sight of the fact that neither the compensation was received by its employer or former employer and nor the stock options scheme was restricted to employees. The stock options had been also allotted to employees of group companies, advisors, consultant etc. A compensation to such diverse group could not be characterised as perquisites or salaries and taxed by implication under the head 'salaries'.

(n) It is therefore clear that while the judgment of the Division Bench of the Delhi High Court in ***Sanjay Baweja's case supra*****,** is directly and squarely applicable to the facts of the instant case, the judgment of the learned Single Judge of the Madras High Court in

Nishithkumar's case supra, cannot be relied upon by the respondents – revenue in support of their claim, which cannot be accepted.

(ix) Insofar as the contention of the respondents-revenue that the present petition is not maintainable in the light of the availability of alternative remedy under Section 264 of the I.T.Act is concerned, it is necessary to state that the impugned order having been passed with the approval of the Commissioner and in the absence of any remedy by way of an appeal, the petitioner is entitled to invoke the jurisdiction of this Court under Article 226 of the Constitution of India, particularly when the right to file a revision petition under Section 264 cannot be construed or treated as availability of an equally efficacious and alternative remedy so as to come in the way of this Court exercising its jurisdiction under Article 226 of the Constitution of India and consequently, even this contention urged by the respondents cannot be accepted. In ***Manpowergroup's case supra***, the Delhi High Court held as under:-

> *"18. This Court is of the view that the present writ petition is maintainable as there is no efficacious alternate remedy available to the petitioner to challenge the*

impugned order. In fact, the Commissioner of Income Tax can entertain a revision petition under section 264 only when the order, which is the subject matter of revision is passed by an authority subordinate to him. Further, the Notification No. 08/2018 dated 31st December, 2018 issued by the CBDT mandates that the decision under section 197 with effect from 31st December, 2018 has to be taken by the Commissioner i.e. after a conscious application of mind. It has also been unequivocally admitted by respondent in para 7 of the impugned order that approval of higher authorities was taken on the online TRACES portal.

19. Consequently, this Court finds merit in the submission of the petitioner that since the impugned order was passed after an approval from the CIT, it cannot be challenged by way of a revision petition before the CIT under section 264 of the Act. To hold otherwise, would amount to directing the petitioner to file an 'appeal from Caesar to Caesar."

In ***Tata Teleservices's case supra*****,** the Bombay High Court held as under:-

"4. The relevant facts leading to the filing of this Petition are that the Petitioner is engaged in providing telecommunication services. In the course of its business, Petitioner earns its revenue from sale of post and prepaid cards, sale/ lease of equipments and providing various value added services. Petitioner has huge accumulated

losses. Its return of income for the Assessment Years 2014-15 to 2016-17, are loss returns aggregating to Rs. 1330.00 Crores and in which an aggregate claim to a refund of Rs. 121.00 Crores has been made.

5. In the course of its business, Petitioner receives various payments for services rendered which are subject to tax deduction at source under Chapter XVII of the Act. However, according to the Petitioner it would not be liable to pay corporate tax in the immediate future in view of the likely loss for the assessment year 2018-19 and the huge carried forward losses.

6. Therefore, on 27 February 2017, Petitioners applied to the Respondent No. 1 seeking an issuance of nil/lower withholding taxes under Section 197 of the Act. This was to enable the Petitioner to receive its payments from various parties which are subject to tax deduction at source, without deduction at source. In support of the above, the application pointed out that their accumulated losses carried forward as on 1 April 2014 is over Rs. 4000.00 Crores – both as per MAT provisions and under the normal provisions. Further, the Petitioner had filed loss returns for Assessment Years 2015-16 and 2016-17. It was also submitted that the estimated loss for Assessment Year 2017-18 is approx. Rs. 1000.00 Crores. Thus, there will be no assessable profit under the Act for the assessment year in 2018-19 in view of huge carry forward losses. Besides, the application points out that there was an amount of Rs. 101.53 Crores up to 10 February 2017 receivable as refund from the Revenue. It

was also pointed out that the financial health of the Petitioner is such that it has taken long term debts, at huge interest payments. Therefore, the amounts which are blocked on account of tax deduction at source aggravates its financial hardship including cash crunch. Lastly, it was pointed out that the amount of Rs. 6.68 Crores which is the outstanding tax demand for the assessment year 2012-13 was on account of an issue which already stands concluded in its favour by an order of the Tribunal dated 27 May 2016, on identical issues for assessment years 2009-10 to 2012-13 (upto July 2011). This demand of Rs. 6.68 Crores is thus, likely to be set aside by the CIT(A) as he would be bound by the order of the Tribunal. It was pointed out so far as the demand for the balance amount of Rs. 28.00 Lakhs is concerned it is on account of wrong/unsustainable demand arising from an incorrect processing of TDS statement on application of TRACES System.

7. Thereafter, Respondent No. 1 called for various details from the Petitioner. On the same being submitted, they were examined by Respondent No. 1. Thereafter, on 4 May 2017, Respondent No. 1 issued a certificate under Section 197 of the Act, directing the deduction of tax at nil rate by the various persons listed in the certificate while making payments to the Petitioner under Sections 194, 194A, 194C, 194I, 194H and 194J of the Act. This would result in a relief of Rs. 238.90 Crores as the same would not be deducted as tax at source. Thus, obviating the

need for filing of refund claim with the Revenue for the assessment year 2018-19.

8. Thereafter, on 16 August 2017, Respondent No. 1 informed the Petitioner that he is reviewing cases where certificate under Section 197 of the Act has been issued in cases where huge outstanding tax demand is pending. Consequently, the above communication requested the Petitioner to furnish the details of outstanding tax demands. The Petitioner responded to the same by its letter dated 20 August 2017, giving the details of the tax outstanding. It reiterated its submissions made in the application made on 27 February 2017. Besides pointing out that a further refund of Rs. 34.37 Crores was due to them from the Revenue for tax deducted at source in the subject assessment year, for the period prior to the issue of certificate.

9. Thereafter, on 30 August 2017, Respondent No. 1 issued a Show Cause Notice to the Petitioner, calling upon it to show cause as to why the certificate dated 4 May 2017 should not be reviewed/ canceled. This was on account of outstanding demand of taxes payable. Besides, relying upon the extract of Central Action Plan 2017-18 issued by CBDT which directs the Officers to follow the instructions/certificate issued by the CBDT and also mentions of Certificates being issued where large demands are pending. The Petitioner responded by letter dated 7 September 2017 to the notice dated 30 August

2017 while reiterating its reply dated 20 August 2017 and called for withdrawal of the notice.

10. Thereafter, on 7 September 2017, a personal hearing was granted and on 23 October 2017, the impugned order was issued. By the impugned order, the certificate dated 4 May 2017 issued under Section 197 of the Act, was canceled. The impugned order holds that while issuing the certificate dated 4 May 2017 the existing demand of Rs. 6.90 Crores was as recorded in the impugned order "Apparently, the demand was not considered on the basis that this demand was under a covered issue". This i.e "covered issue" in terms of Rule 28AA(2) of the Income Tax Rules 1961 (Rules), cannot be a subject of consideration while granting the certificate. Further, it holds that in view of the current financial status, the future liability, if any, which may arise on assessment or otherwise against the company, would be impossible to recover.

11. Before considering the rival submissions urged on behalf of the respective parties, it would be useful to reproduce Section 197 of the Act and Rule 28AA of the Rules, which arises for our consideration:—

*"**Section 197 of the Act** :—*

(1) Subject to rules made under sub-section (2A), where, in the case of any income of any person or sum payable to any person, income-tax is required to be deducted at the time of credit or, as the case may be, at the time of payment at the rates in force under the provisions of

sections 192, 193, 194, 194A, 194C, 194D, 194G, 194H, 194-I, 194J, 194K, 194LA and 195, the Assessing Officer is satisfied] that the total income of the recipient justifies the deduction of income-tax at any lower rates or no deduction of income-tax, as the case may be, the Assessing Officer shall, on an application made by the assessee in this behalf, give to him such certificate as may be appropriate.

(2) Where any such certificate is given, the person responsible for paying the income shall, until such certificate is cancelled by the Assessing Officer, deduct income-tax at the rates specified in such certificate or deduct no tax, as the case may be.

(2A) The Board may, having regard to the convenience of assessees and the interests of revenue, by notification in the Official Gazette, make rules specifying the cases in which, and the circumstances under which, an application may be made for the grant of a certificate under sub-section (1) and the conditions subject to which such certificate may be granted and providing for all other matters connected therewith.

Rule 28AA- Certificate for deduction at lower rates or no deduction of tax from income other than dividends.—

(1) Where the Assessing Officer, on an application made by a person under sub-rule (1) of rule 28 is satisfied that existing and estimated tax liability of a person justifies the deduction of tax at lower rate or no deduction of tax, as

the case may be, the Assessing Officer shall issue a certificate in accordance with the provisions of sub-section (1) of section 197 for deduction of tax at such lower rate or no deduction of tax.

(2) The existing and estimated liability referred to in sub-rule (1) shall be determined by the Assessing Officer after taking into consideration the following:-

(i) tax payable on estimated income of the previous year relevant to the assessment year;

(ii) tax payable on the assessed or returned income, as the case may be, of the last three previous years;

(iii) existing liability under the Income-tax Act, 1961 and Wealth-tax Act, 1957;

(iv) advance tax payment for the assessment year relevant to the previous year till the date of making application under sub-rule (1) of rule 28;

(v) tax deducted at source for the assessment year relevant to the previous year till the date of making application under sub-rule (1) of rule 28;

and

(vi) tax collected at source for the assessment year relevant to the previous year till the date of making application under sub-rule (1) of rule 28.

(3) The certificate shall be valid for such period of the previous year as may be specified in the certificate, unless it is cancelled by the Assessing Officer at any time before the expiry of the specified period.

(4) The certificate for no deduction of tax shall be valid only with regard to the person responsible for deducting the tax and named therein.

(5) The certificate referred to in sub-rule (4) shall be issued direct to the person responsible for deducting the tax under advice to the person who made an application for issue of such certificate."

12. *Mr. Tarun Gulati, learned Counsel, in support of the Petition, submits as under:—*

(a) The impugned order dated 23 October 2017 cancelling the certificate dated 4 May 2017, is without jurisdiction as Rule 28AA(3) of the Rules could not be invoked in the present facts;

(b) The impugned order is arbitrary as it cancels a valid certificate under Section 197 of the Act, ignoring the fact that the existing liability of the Petitioner would continue to be nil on consideration of the factors as provided under Rule 28AA(2) of the Rules;

(c) The impugned order completely ignores the test of proportionality. At the highest, according to the Revenue, the unpaid tax demand is Rs. 6.90 Crores. While undisputedly, Petitioner is entitled to refund of

Rs. 7.30 Crores (being the deposit made), consequent to the order dated 27 May 2016 passed by the Tribunal in respect of Assessment Years 2009-10 to 2012-13. The aforesaid amount continues to be retained by the Revenue and it could be easily adjusted against the demand of Rs. 6.90 Crores. In any event, the relatively meagre amount of Rs. 6.90 Crores of tax demand as against a refund of over Rs. 121.00 Crores would not justify denial of the benefit of about Rs. 238.00 Crores as available under Section 197 of the Act. ;

(d) Lastly, it is submitted that the amount of Rs. 6.68 Crores is on account of an order for Assessment Year 2012-13 which is pending before the CIT(A). This issue to the knowledge of all concerned is concluded in favour of the Petitioner and kept pending deliberately. This, even after the hearing was completed, so far back as in February 2017.

13. *On the other hand, Mr. Suresh Kumar, learned Counsel for the Revenue supports the impugned order dated 23 October 2017 and submits as under:-*

(a) An equally efficacious alternative remedy under Section 264 of the Act as an by way of a Revision to be Commissioner of Income Tax (CIT), against the impugned order dated 23 October 2017, cancelling the certificate dated 4 May 2017 is available to the Petitioner. Therefore, this Court should not entertain the Petition to exercise its extraordinary jurisdiction;

(b) Cancellation of the certificate dated 4 May 2017 became necessary in view of the fact that the financial condition of the Petitioner-company has further deteriorated. Thus, putting in jeopardy the recovery of any liability, which may arise against the Petitioner-company on account of future assessment or otherwise. Therefore, necessitating the cancellation of the nil withholding tax certificate dated 4 May 2017;

(c) The existing demand of Rs. 6.90 Crores which continued to be pending. This cannot be ignored merely because, according to the Petitioner, the demand is unsustainable and would be set aside in appeal due to the issue being considered in its favour;

(d) No prejudice would be caused to the Petitioner in case the nil withholding certificate dated 4 May 2017 is withdrawn. This, for the reason that the amounts so received by the Revenue on account of withholding tax would be refunded if no tax demand is payable in future by the Petitioner.

14. Before dealing with the rival submissions on merits, we shall first deal with the preliminary objection of the Respondent to entertain this Petition. The objection is that an effective efficacious alternative remedy to challenge the impugned order under Section 264 of the Act, is available. Therefore, this Petition should not be entertained. It is submitted that a Revision under Section 264 of the Act would lie to the Commissioner of Income Tax (CIT). This is so for the reason that under Section 264 of the Act, Revision lies from any order passed by any authority – subordinate to CIT

other than an order which is appealable and from which an appeal has been filed or an order to which Section 263 of the Act is applicable. In fact, this Court in Larsen & Toubro Ltd. v. Asstt. CIT[2010] 326 ITR 514/190 Taxman 373 (Bom.) has held that an order passed under Section 197 of the Act, is amenable to Revision under Section 264 of the Act.

15. However, as correctly pointed out by the Petitioner in this case, the impugned order dated 23 October 2017 as recorded therein, has been issued/ decided with the concurrence of the CIT (TDS). This was not so in the case of Larsen & Toubro Ltd. (supra). It is also not disputed before us that in this case, the Revision would be before the same authority who gave the concurrence or to an authority of equal rank/designation.

16. In the above view, the decision of this Court in Larsen & Toubro Ltd., (supra) would not apply to the present facts. As in this case, the Revision i.e. alternative remedy would in facts be from "Caesar to Caesar." Therefore, in such a case an alternative remedy would be a futile/empty formality and not an efficacious remedy. (Please see Ram & Shyam Co. v. State of Haryana [1985] 3 SCC 267).

8. In view of the aforesaid facts and circumstances, I am of the considered opinion that the 1st respondent clearly fell in error in rejecting the application filed by the petitioner seeking issuance of 'Nil Tax Deduction Certificate' in relation to the subject

compensation amount of Rs.71,01,004/- by passing the impugned order which is illegal, arbitrary and contrary to facts and law as well as the aforesaid principles and statutory provisions and consequently, the impugned order deserves to be set aside and the application filed by the petitioner deserves to be allowed by directing the respondents to issue 'Nil Tax Deduction Certificate' in favour of the petitioner within a stipulated timeframe.

9. In the result, I pass the following:-

ORDER

(i) Petition is hereby allowed.

(ii) The impugned order at Annexure-A dated 02.08.2023 passed by the 1st respondent is hereby quashed.

(iii) The respondents are directed to issue 'Nil Tax Deduction Certificate' in favour of the petitioner as sought for by him together with all consequential benefits flowing therefrom as expeditiously as possible and at any rate, within a period of six weeks from the date of receipt of a copy of this order.

Sd/-
(S.R.KRISHNA KUMAR)
JUDGE

Srl.