Commissioner of Income-Tax, Madhya Pradesh and Bhopal

Vs

Vyas and Dhotiwala

Civil Appeal No. 222 of 1956

(T. L. Venkatarama Ayyar, P. B. Gajendragadkar, A. K. Sarkar JJ)

03.10.1958

JUDGMENT

SARKAR, J. -

This is an appeal brought by special leave against the judgment of the High Court at Nagpur, delivered on a reference under section 66(1) of the Income-tax Act. The appeal is by the Commissioner of Income-tax, Madhya Pradesh and Bhopal. The respondents are the assessees Vyas and Dhotiwala. The respondents have not appeared in this appeal. We shall presently set out the facts but before we do that, we wish to state that the assessment years concerned were 1945- 46 and 1946-47. Though there were two separate assessment orders in respect of these years, ultimately when they came up before the Appellate Tribunal they were consolidated into one appeal. The appeal before us likewise concerns both these assessment years.

It appears that in or about July, 1943, when considerable difficulty was being felt about cloth, the Deputy Commissioner, Amraoti, evolved a scheme to solve that difficulty. Under that scheme Kisanlal Vyas and a firm called Edulji Framji Dhotiwala, who have in these proceedings been referred to as Dhotiwala, undertook to finance the scheme without charging any interest on profit and were appointed as financiers and also distributors of a variety of cloth called standard cloth for the town and camp of Amraoti and certain areas in the interior. It is not necessary to set out the various details of the scheme and it will be sufficient to state that Vyas and Dhotiwala, who as an association of person are the assessees concerned, agreed to open an account in the Imperial Bank of India to be operated by them out of which the purchases of the cloth were to be financed. The orders for the cloth were to be placed by the Government with the mills and on the arrival of a consignment of cloth, the assessees were to pay to the Deputy Commissioner Amraoti, the values of the consignment together with 6 1/4 per cent. of the ex-mill price. The consignment was thereupon to be opened and its contents check by the assessees and the official and delivered to the assessees on their granting a receipt for the same. The Deputy Commissioner would pay 4 1/2 per cent. of the ex-mill price to the assessees out of the amount paid by the latter as aforesaid for contingent expenses of working the scheme. The scheme provided that the contingent expenses were not to exceed 3 per cent. of the ex-mill price. The cloth coming to the hands of the assessees was to be distributed in Amraoti town and the camp through a shop to be opened by the assessees and in the interiors of the area concerned through Tehsildars with Patils under them. The substance of the arrangement of distribution appears to have been that it would be entirely under the control of the Deputy Commissioner who made himself responsible to the assessees for the sale proceeds receivable from the Tehsildars. The Deputy Commissioner was to decide the price for which the cloth was to be sold to the consumers and also the persons entitled to buy the cloth. Out of the sale proceeds the Deputy Commissioner was to pay to the assessees whatever they had advanced on

account of the cloth. The most important provision in this scheme is paragraph 14 which is set out below.

> "Profits resulting from the scheme shall be utilised for such charitable purposes as may be decided on by the Deputy Commissioner in consolation with the advisory committee appointed to supervise the scheme."

It appears that the books of the assessees showed Rs. 34,737 for the assessment year 1945-46 and Rs. 17,682 for the assessment year 1946-47 as profits earned in working the scheme. The Income-tax Officer assessed the assessees to tax on the profits so earned. The assessment orders made by this officer would appear to show that the only point urged by the assessees before him against the assessment was that the income was exempt from taxation under section 4(3) (i-a) of the Indian Income-tax Act, 1922. The officer rejected this contention. The assessees went up in appeal to the Appellate Assistant Commissioner, before whom the same contention appears to have been repeated. The Appellate Commissioner confirmed the order of the Income-tax Officer. The assessees then appealed to the Appellate Tribunal. The Tribunal held that the assessees had objected to the assessment before the Income-tax Officer on two grounds, namely that the income was not the income of the assessees and that the income was exempt from taxation under section 4(3) (i-a), as appeared from their letter dated January 22, 1947. One of these alone had been dealt with by that officer, as appears from his order earlier referred to. The Appellate Tribunal agreed with the contention of the assessees that they were not liable to be taxed on the profits because these did not form their income. The Tribunal was of the view that the scheme was the scheme of the Deputy Commissioner and completely under his control; that the assessees were merely the financiers and also managers under the Deputy Commissioner to carry out the scheme and that the assessees only helped to work the scheme. The Tribunal held that the profits that may have resulted from such working were not therefore theirs, nor represented their income and the assessees could not be assessed to income-tax thereon. In this view of the matter the Tribunal set aside the orders of assessment.

Thereafter, on the application of the revenue authorities the Tribunal referred the following question to the High Court under section 66(1) of the Act :

> "Whether on the facts of this case any income accrued to Messrs. Vyas and Dhotiwala as the result of their associating themselves as financiers in the scheme for the distribution of standard cloth; and, if so, whether such income was assessable in their hands ?"

On that reference the High Court held that under the charging section in the Indian Income-tax Act, 1922, namely, section 4, it was necessary for the revenue authorities to prove that the assessees received or should be deemed to have received income or profit from the scheme during the relevant period. It held that the assessees had not actually received any such income and further that the expression "deemed to be received" in that section only meant deemed by the provisions of the Act to be received, and no such provisions of the Act had been relied upon on behalf of the revenue authorities. In this view of the matter the High Court answered the question framed in the negative.

The learned Solicitor-General contends that the High Court failed to appreciate the real question. He says that the question was not whether income was received or deemed to be received but whether income had accrued and the point for decision was, as appeared from the judgment of the Tribunal, whether the profits formed the income of the assessees. We agree with this criticism of the judgment

of the High Court.

On the point that arises from the question framed, we think that the Tribunal went wrong. It is not disputed that the assessees worked the scheme and such working produced the profits as found in the assessment orders. The Tribunal thought that since the scheme was completely under the control of the Deputy Commissioner, the assessees could not be said to have carried on business carried on business by working the scheme. We are unable to see that the fact of the control of the Deputy Commissioner can prevent the working of the scheme by the assessees from being a business carried on by them. In our view, it only comes to this that the assessee had agreed to do business in a certain manner. The fact that the Deputy Commissioner guaranteed the payment by the Tehsildars of the price due from them to the assessees would indicate the assessees were treated as the owners of the business. It would indicate that if there had been no such guarantee, the loss due to the failure of the Tehsildars to pay their dues would have to be borne by the assessees. Again the claim, may be in the alternative, by the assessees for exemption under section 4(3) (i-a) would not arise unless the assessees were carrying on a business. Lastly, paragraph 14 of the scheme, which we have earlier set out, clearly contemplates profit resulting from the scheme. The provision that the profits would be devoted to charity to be decided by the Deputy Commissioner, would indicate that without it the profits would have been utilisable by the assessees. The profits belonged to the assessees and hence the necessity for this agreement so that the assessees might be made to spend them on charity. If, as the Tribunal thought, the profits were of the Government, there was no necessity for the Government providing for the profits being expended on charity, for the Government, if minded to do so, could have done it without such a provision. The fact remains that the working of the scheme produced profits an apart from paragraph 14 such profits undoubtedly belonged to the assessed. If they chose to agree by paragraph 14 to devote the profits to charity, that was their business; the profits made by them would not change their character and cease to be the assessees' income because they agreed to devote their income to charity. We might also say that there is nothing in the scheme which shows that the assessees had undertaken not to make any profits on the distribution work under the scheme; they had only agreed to finance the scheme without receiving any interest or profit. Furthermore, since the assessees actually made the profits, they are liable to pay tax thereon whether they agreed not to make any profits or not. We wish also to point out that it is not the assessees' case that they have been made to pay out the profits for any charity. For these reasons we think that the profits were the profits of the assessees and they are liable to pay tax on them.

With regard to the assessees' claim for exemption under section 4(3) (i-a), they are clearly not entitled to any. That claim of the assessees has not been accepted by any of the courts below. Section 4(3) (i-a) applies to income derived from business carried on on behalf of religious and charitable institution when the income is applied solely to the purpose of the institution and the business is carried on in the manner provided. It is enough to say that the scheme, considered as a business, was not carried on on behalf of any religious or charitable institution. Once it is held that the assessees made the profits, how they use it would not matter.

In the result, we would answer both parts of the question framed, in the affirmative. We hold that the profits were the income which accrued to the assessees and such income is assessable to income-tax and is not exempt from taxation under section 4(3) (i-a). The appeal is allowed with costs here and below.

Appeal allowed.

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