

Commissioner of Income Tax

Vs

Ambat Echukutty Menon

Civil Appeals Nos. 2242-2247 of 1972

(N.L. Untwalia, R.S. Pathak JJ)

06.09.1979

JUDGMENT

UNTWALIA, J. -

1. These six appeals by special leave preferred by the Commissioner of Income Tax from the Judgments of the Kerala High Court are all inter-connected and arise but of different proceedings in relation to one assessment year only. They have, therefore, been heard together and are being disposed of by this judgment.

2. The assessee-respondent is a Hindu undivided family owning large agricultural lands in the State of Kerala. In 1905 the family purchased in court auction some lands covering an area of about 200 acres. There were two irrigational channels in the land drawing water from a river. According to the sanad, there were about 772 trees of various kinds like Karimpana, coconut trees, jack trees, tamarind trees, Maruthu, etc. There were other trees of spontaneous growth but they were not in one block. They were interspersed among the paddy fields as the land aforesaid was meant for paddy cultivation. By an agreement dated November 28, 1960 the assessee sold to one Velappa Rowther trees from about 60 acres of land forming part of the 200 acres aforesaid. Since the original term stipulated in connection with the payment of money by Rowther could not be adhered to by him, further agreements were entered into deferring and spreading the payments over some years. The assessee under the impression that the money which it received from Rowther on account of sale of trees was not chargeable to income tax under the Indian Income Tax Act did not file any voluntary return. On February 28, 1963 the Income Tax Officer, Palghat wrote to the Karanavan of the assessee family pointing out that he had information that the assessee had leased certain private forests to Velappa Rowther for cutting timber; and that the assessee had received Rs. 75,000 during the relevant year. The corresponding assessment year would be 1961-62. The assessee was asked to explain why no voluntary return had been filed. In reply to the letter of the Income Tax Officer the assessee wrote a letter dated April 3, 1963 stating therein that there was no lease but an out and out sale of the entire standing timber trees except certain specified varieties and that the sale was effected with a view to extend wet or dry cultivation in its field in the area; the receipt therefrom were of a capital nature or in any event it was an agricultural income. The assessee, however, concluded its letter by stating that he had no deliberate intention of avoiding to file any return. If the Income Tax Officer so desired, he was ready to comply with his direction.

3. Thereafter the Income Tax Officer served a notice on the assessee under Section 148 of the Income Tax Act, 1961, hereinafter called the Act. In response to the same the assessee filed a return on March 25, 1966 showing a total net income of Rs. 626.63 paise for the previous year ending on March 31, 1961. The Income Tax Officer held that out of the total number of trees numbering 772

four varieties were not sold and roughly speaking the number of trees sold and allowed to be cut as per the agreements came to 367. The trees were of spontaneous growth and the whole of the amount of Rs. 1,75,000, although the whole of it was not paid during the accounting year, represent the assessee's income which had accrued as per the terms of the agreement in that very year. He accordingly assessed the whole of the amount to income tax.

4. The Appellate Assistant Commissioner allowed the appeal of the assessee in part and held that only a sum of Rs. 75,000, the amount actually received during the accounting year, was assessable to income tax in the assessment year 1961-62. The assessee as well as the department both preferred appeals before the Income Tax Appellate Tribunal from the order of the Appellate Assistant Commissioner. The Tribunal by its order dated November 16, 1968 dismissed both the appeals.

5. At the instance of the assessee the Tribunal stated a case which was numbered as Reference No. 30 of 1970 and referred the following question of law to the High Court for its opinion :

Whether, on the facts and in the circumstances of the case, the receipts from the sale of trees of spontaneous growth were assessable to tax and if so, whether assessable under 'Other Sources' ?

The High Court by its judgment, since reported in *Ambat Echukutty Menon v. CIT* ((1973) 87 ITR 129 (Ker HC)) has answered the question in the negative, in favour of the assessee and against the department. Civil Appeal No. 2247 arises out of Reference No. 30 of 1970.

6. At the instance of the Revenue also the Tribunal made a reference being Reference No. 29 of 1970 and the question of law referred to the High Court is in the following terms :

Whether on the fact and in the circumstance of the case, the whole of the sum of Rs. 1,75,000 was not assessable to tax in the previous year ending on March 31, 1961 relevant for the assessment year 1961-62.

Since the High Court in the main reference opined that the receipt from the sale of the trees were of a capital nature, this reference was also answered in favour of the assessee. Civil Appeal No. 2242 arises out of Reference No. 29 of 1970.

7. The Income Tax Officer initiated penalty proceedings against the assessee, one under Section 271(1)(a) of the Act and the other under Section 273(b), the former being for the alleged failure of the assessee to furnish the return for the period in question and the latter for its alleged failure to furnish an estimate of the advance tax payable. In relation to the penalty proceedings under Section 271(1)(a) of the Act, two reference were made to the High Court, one at the instance of the Revenue and the other at the assessee's instance and two reference were similarly made in relation to the penalty proceeding under Section 273(b). As a consequence of the main judgment of the High Court in Reference No. 30 of 1970 all these four references also had to be disposed of in favour of the assessee. Civil Appeals 2243 to Civil Appeals 2246 have been preferred by the department in these penalty proceedings.

8. Since, in our view, for the reasons to be stated hereinafter the judgment of the High Court in the main reference giving rise to Civil Appeal 2247 is correct and the said appeal has to fail on that account, it is plain that the other five appeals fail as a corollary to the same and have got to be dismissed as such. I now proceed to discuss and decide the relevant question of law in the main appeal.

9. Before I notice and advert to some special facts of this case it would be better to have a resume of some decisions of the High Courts and this Court taking one view or the other in relation to the sale of trees, some cases holding that it is a capital receipt and some cases concluding in different situations and on different facts that it is a revenue receipt. In *CIT v. T. Manavedan Tirumalpad* (ILR 54 Mad 21 : AIR 1930 Mad 764) a Full Bench of the Madras High Court held that the receipts from the sale of timber trees by the owner of unassessed forest lands in Malabar were chargeable to income tax. Such trees were treated as usufruct from the land like paddy from land and minerals from mines. Similarly the Oudh Chief Court expressed the view in *Maharaja of Kapurthala v. CIT* ((1945) 13 ITR 74 (Oudh HC)) that the net receipt from the sale of forest trees are income liable to income tax even though the forest would be gradually exhausted by fellings. This was a case of forest trees of spontaneous growth growing on land which was assessed to land revenue. The Patna case, *via. Raja Bahadur Kamakshya Narain Singh v. CIT* ((1946) 14 ITR 673 (Pat HC)) was also a case of the receipts from the sale of forest trees. In *Fringford Estates Ltd., Calicut v. CIT* ((1951) 20 ITR 385 (Mad HC)) the sale of timber comprised in the trees from the forest was on a business line and the profits derived from the same were held to be assessable to income tax on the principle that profits derived from capital which is consumed or exhausted in the process of realization are nonetheless the taxable income.

10. The other cases taking the view that money received by sale of trees is a capital receipt are of the nature where trees have not been treated as usufruct of the land. They were treated as part of the capital assets and the receipts from the sale of such trees retained the same character. In *CIT v. N. T. Patwardhan* ((1961) 41 ITR 313 (Bom HC)) the Bombay High Court was dealing with a case of the sale once for all of the trees with roots even though they were of the spontaneous growth. The receipts from such sales were held to be capital in nature. The Kerala High court in *State of Kerala v. Karimtharuvi Tea Estate Ltd.* ((1964) 51 ITR 129 (Ker HC)) was concerned with the sale of firewood of gravelia trees grown and maintained in tea gardens for the purpose of affording shade to tea plants. Even sale proceeds of forest trees felled for the purpose of coffee plantation in the land were held to be capital receipts by the Mysore High Court in the case of *CIT. v. H. B. Van Ingen* ((1964) 53 ITR 681 (Mys HC)) and the Madras High Court in the case of *CIT v. M. S. P. Nadar Sons* ((1973) 87 ITR 202 (Mad HC)). Similarly sale of dead and wind-fallen trees and trees planted for shade were held to be bringing receipts of capital nature *vide Elixir Plantations Ltd. v. CIT* ((1969) 71 ITR 741 (Ker HC) and *Consolidated Coffee Estate, (1943) Ltd. v. C. Ag. I. T.* ((1970) 76 ITR 29 (Mys HC)).

11. In *CIT v. Venugopala Varma Raja* ((1968) 67 ITR 802 (Ker HC)) the Kerala High Court was concerned with the trees of spontaneous growth. Obviously the income was not agricultural income. The owner of a forest had derived income from a lease of the forest which came within the ambit of the Madras Preservation of Private Forests Act, 1949. The lease was for "clear felling" which had a definite and specific meaning under Rule 7 framed under the said Act. It did not permit a removal of the trees along with their roots. The felling of the trees had to be done in such a way as to permit the regeneration and future growth of the trees concerned. "In other words, what is contemplated by the clear felling method is not the sterilisation of an asset but the removal of a growth above a particular height, leaving intact the roots and the stumps in such a manner as to ensure regeneration, future growth, further felling and a subsequent income" (page 803). On that account it was held that it was a revenue receipt and not a capital one. The case came up to this Court and the view of the High Court was eventually upheld. The decision of this court is reported in *v. Venugopala Varma Rajah v. CIT.* ((1970) 1 SCC 43 : (1970) 76 ITR 460) A supplementary statement of the case was called for by this Court but ultimately the decision turned round the true import of the expression "clear felling". Some of the earlier decisions of the various High Courts noticed by me above were referred

and it was thought that there was some conflict between them, yet finally without resolving the conflict, the view expressed at page 466 by this Court with reference to the facts of the case was in these terms : (SCC p. 46, para 10)

It is not necessary for the purpose of this case to enter upon a detailed analysis of the principle underlying the decisions and to resolve the conflict. On the finding in the present case it is clear that the trees were not removed with roots. The stumps of the trees were allowed to remain in the land so that the trees may regenerate. If a person sells merely leaves or fruit of the trees or even branches of the trees it would be difficult [subject to the special exemption under Section 4(3) (viii) of the Indian Income Tax Act, 1922] to hold that the realization is not of the nature of income. Where the trunks are cut so that the stumps remain intact and capable of regeneration, receipts from sale of the trunks would be in the nature of income. It is true that the tree is a part of the land. But by selling a part of the trunk, the assessee does not necessarily realise a part of his capital. We need not consider whether in case there is a sale of the trees with the roots so that there is no possibility of regeneration, it may be said that the realization is in the nature of capital. That question does not arise in the present case.

12. The question, however, of sale of trees with roots arose before this Court shortly after in A. K. T. K. M. Vishnudatta Andharjanam v. C. Ag. I. T. ((1970) 2 SCC 165 : (1970) 78 ITR 58) Shah, J., as he then was, who had delivered the judgment in Venugopala's case ((1970) 1 SCC 43 : (1970) 76 ITR 460) was a party in this case also, the judgment of which was delivered by Grover, J. The test laid down by the Privy Council in CIT v. Shaw Wallace and Co. ((1932) 2 Com Cas 276 : 6 ITC 178 : AIR 1932 PC 138) was applied and it was said at page 61 : (SCC p. 167, para 4)

According to that test, income 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. Once the teak trees were removed together with their roots and there was no prospect of regeneration or of any production of a return therefrom it could well be said that the source ceased to be one which could produce any income.

I am aware that the test laid down by Sir. George Lowndes in Shaw Wallace case ((1932) 2 Com Cas 276 : 6 ITC 178 : AIR 1932 PC 138) has been whittled down to a very large extent by subsequent pronouncements of the Privy Council, e.g. in Gopal Saran Narain Singh v. CIT ((1935) 3 ITR 237 (PC) and Kamakshya Narain Singh v. CIT ((1943) 11 ITR 513 (PC)) yet in the matter of sale of trees when this Court applied the same test in Vishnudatta's case ((1970) 2 SCC 165 : (1970) 78 ITR 58) it was for the purpose of lying stress on the object of the felling of the trees. The return may be one and only one. But if the object of felling the trees leaving the roots and stumps intact is for regeneration of income, then whether income is regenerated or not is immaterial. But in a case where the trees are sold by uprooting the roots nobody can say that there could be any object of regeneration of income from the trees growing again as there was no question of a second growth at all. Similarly, ordinarily and generally, when the trees are sold and allowed to be felled by leaving the roots and stumps intact then in case of trees of spontaneous growth there is a likelihood of fresh sprouting and further growth of trees on the left out roots and stumps. The presumption in such cases generally would be that the owner did it with the object of regenerating the income. But there may be cases, although few and far between, like the one with which we are concerned here where

the roots and stumps were not allowed to be uprooted and cut by the licensee or the lessee yet the object was not the regeneration of the trees but a protection of the land eventually to be used for the purpose of cultivation. In this background of the law, I now proceed to refer to the special facts of this case.

13. Clauses 12 and 13 of the agreement dated November 28, 1960 entered into between the assessee and Velappa Rowther are as follows :

(12) The trees in the reared forest have to but (sic be) cut neatly and the relative stumps should not be either pulled out or cut out.

(13) No. 3 should not enter on the lands from where trees are cut or on the sprouts coming up from there. After the cuttings sprouts are not to be cut.

No. 3 referred in clause (13) is the said Rowther. On the face of the agreement, therefore, the transaction was not a sale of trees with roots and stumps. Rather there was a prohibition that after the cutting, sprouts were not to be cut. The agreement, however, did not indicate as to what was the object of the assessee in incorporating clauses (12) and (13) in the agreement. Was it the regeneration of the trees for earning more income or was it something else ? The subsequent conduct of the assessee as appeared from the facts placed before the income tax authorities without anything more will indicate that the object of the assessee was to protect the land falling vacant after the cutting of the trees from being damaged by the licensee by at random cutting of the stumps and uprooting of the roots. The trees sold were spread in an area of 60 acres of land only. Even in that area the trees were not in any thick or continuous forest. They were interspersed by paddy fields. In its very first communication to the Income Tax Officer sent on April 3, 1963, the assessee perhaps was made aware of the decision of the Kerala High Court in CIT v. Venugopala Varma Rajah ((1968) 67 ITR 802 (Ker HC) which was a case of private forest governed by the Madras Act. The assessee, therefore, claimed that there were no private forests in Cochin area of Kerala where the land was situated. The assessee asserted that in substance and in effect the sale was of the entire standing timber, i.e. totality of the trees and "the sale was effect with a view to extend wet or dry cultivation to that area as well since the standing trees were a hindrance for such extension". In this very letter the assessee also asserted :

This is the very first time that our Thavazhi has sold the trees. The trees, the subject-matter of the sale contract, were there at the time of the purchase of the agricultural lands by our Thavazhi in 1080 M.E. The trees were old trees. No tree had been sold after our Thavazhi became the owner of the agricultural lands. A large extent of agricultural lands was purchased and these trees formed part and parcel of such holdings. None of us know when the trees began to grow. After purchase of the lands we had developed the same and in the process we sold the trees with the object mentioned above. The present sale has been the only sale and it will be the last one also since our idea is to extend cultivation to this area as well.

14. The Tribunal in its appellate order noticed the argument of the assessee that its sole occupation was agriculture and the attraction in the purchase of the land in the year 1905 was two irrigational channels contained therein. It also noticed the other facts stated in the letter aforesaid of the assessee and finally concluded on the basis of clauses (12) and (13) of the agreement : "It is clear from these that the assessee was reserving to itself the results of the future growth and a source of income". The case was squarely covered, in its opinion, by the decision of the Kerala High Court in Venugopala's

case ((1968) 67 ITR 802 (Ker HC)). It further observed that the assessee was claiming exemption and it was up to him to furnish all the information as to what trees would not regenerate, what kind of trees were sold, etc. The assessee had failed to furnish these details. Yet it would be noticed that without rejecting the assessee's stand that the transaction in question was the first and the last sale of trees by the assessee and without finding that the object of the assessee was not to convert the land for cultivation but to earn income by regeneration of trees, it upheld the view of the departmental authorities that the receipt was a revenue receipt assessable to income tax. It should be noted that the assessment made was not for default of the assessee to produce any relevant material but a regular assessment on consideration of such materials as were produced by it. It was not asked to produce any other evidence or material to substantiate the stand by it. Nor was the stand rejected. In such a situation it was not a question of assessee's claiming any exemption and failing to get it for its alleged failure to furnish any more details. But it was a case where in order to net the receipt as a revenue receipt it was for the department to reject the assessee's stand and to hold that the object of the assessee in not allowing the licensee to cut the stumps and uproot was a regeneration of the income. The High Court has also noticed the fact as found mentioned in the order of the Tribunal that by the time the assessment was completed by the Income Tax Officer and area of 10 acres had been converted into cultivable land. In our opinion, therefore, the High Court rightly distinguished the decision in Venugopala's case ((1968) 67 ITR 802 (Ker HC)) and applied the ratio of that of Vishnudatta's case ((1968) 67 ITR 802 (Ker HC)). As I have observed above the facts of this case were on a line which on the surface was blurred and indistinct, yet, on a careful examination of the matter I find that the dividing line, though thin, nonetheless, is distinct enough to make this case fit for application of the ratio of the decision of this Court in Vishnudatta's case ((1968) 67 ITR 802 (Ker HC)). I accordingly uphold the view of the High Court.

15. In the result all the six appeals are dismissed but on the special facts and circumstances of this case we make no order as to costs in any of them.

Pathak, J. (concurring) -

I agree with my learned brother that the appeals should be dismissed. And I shall set out my reasons.

17. The case is one where trees of spontaneous growth were sold on condition that the purchase would cut and remove the trunks without disturbing the stumps and roots embedded in the soil. Where trees are so felled and removed, and the stumps and roots are allowed to remain in the land with a view to regeneration of the trees, the intention of the owner would be to indulge in a profit-making activity, and the case would fall within V. Venugopala Varma Rajah v. CIT. ((1970) 1 SCC 43 : (1970) 76 ITR 460) The receipts from sale of the trunks would be revenue receipts. But in the present case there was no intention to reserve the stumps and roots for the purpose of allowing regeneration of the trees. The intention and subsequent conduct of the assessee establishes that the stipulation against removal of the stumps and roots was intended to protect the surface of the land from indiscriminate injury because the land was to be applied to cultivation. Intention is a material factor in such cases, and each case has to be decided on its particular facts. Without evidence of the intention or object behind such a stipulation, the mere fact that the trees were sold without stumps and roots cannot lead to the necessary inference that a profit-making activity was involved. Where the evidence shows that the land had been acquired for the purpose of cultivation, and that the prohibition on the purchaser against removing the stumps and roots was intend to prevent undue interference with the soil, and the assessee did not intend to permit regeneration of the trees, and that he had in fact later put the land to cultivation, the payments received on sale of the trunks

cannot be regarded as taxable income. And yet, the case is distinguishable from the facts in A. K. T. K. M. Vishnudatta Andharjanam v. C. Ag. I. T. ((1970) 2 SCC 165 : (1970) 78 ITR 58) That was a case where the trees were sold with their roots, and it was held by this Court that by removal of the roots the source from which the fresh growth of trees could take place had also been removed and, therefore, the sale of such trees affected the capital structure, and could not give rise to a revenue receipt. In my opinion, the present case does not fall either within V. Venugopala Varma Rajah or A. K. T. K. M. Vishnudatta Andharjanam ((1970) 2 SCC 165 : (1970) 78 ITR 58). It is a case where although the stump and roots remained after the trees were felled and removed by the purchaser, the regeneration of the trees was not to be allowed and, therefore, a profit-making activity could not be spelled out.

18. The appeals are dismissed, but there is no order as to costs.

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