Commissioner of Income Tax, U. P. - II, Lucknow

Vs

Bazpur Co-Operative Sugar Factory Ltd., Bazpur, Distt. Nainital

Civil Appeals Nos. 563 and 564 (NT) of 1975

(CJI R.S. Pathak, S. Natarajan, M.N. Venkatachaliah JJ)

06.05.1988

JUDGMENT

KANIA, J. –

1. This is an appeal against the judgment of a Division Bench of the Allahabad High Court in Income Tax Reference No. 67 of 1969. The appeal has been filed at the instance of the Commissioner of Income Tax, U. P.

2. The relevant facts are as follows :

> The respondent (assessee) is a Co-operative Society registered under the Co-operative Societies Act, 1912. It carries on the business of manufacture and sale of sugar and runs a mill situated at Bazpur. The relevant assessment year is the assessment year 1961-62, corresponding to the accounting year July 1, 1959 to June 30, 1960, which was the relevant co-operative year. The assessee had established a fund called "Loss Equalization and Capital Redemption Reserve Fund". On the opening day of the year of account, namely, July 1, 1959, a sum of Rs. 1,30,196 stood to the credit of this fund. During the relevant accounting year, the respondent society added a sum of Rs. 5,15,863 to this fund by deduction from the price payable by the respondent to its members for the supply of sugarcane received from its members. These deductions were made under the provisions of bye-law 50 of the bye-laws of the respondent society, to which we shall presently come. Bye-law 50 under which the said amount was deducted from the price payable by the respondent to its members for the supply of sugarcane at the relevant time ran as follows :
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> There shall be established a Loss Equalisation and Capital Redemption Reserve Fund in the Society. Every producer shareholder shall deposit every year a sum not less than 32 n.p. and not more than 48 n.p. per quintal of the sugarcane supplied by him to the society as may be determined by the Board. After adjusting the losses, if any, in the working year the deposits shall be allowed to accumulate and utilised for repayment of the initial loan from the Industrial Finance Corporation of India and thereafter for redeeming government share.

The balance of the said deposit after meeting losses shall be used in being converted into share capital in accordance with bye-law 44(xix) and each producer shareholder shall be issued shares of the society of the corresponding value in lieu thereof.

3. During the accounting year, the respondent debited a sum of Rs. 2,34,354 to the said fund by adjusting this amount against the loss brought forward from the previous year, with the result that at the close of the said year on June 30, 1960, the account showed a credit balance of Rs. 4,11,705. A meeting of the sub-committee of the respondent society which was held on August 26, 1964 took the view that bye-law 50 was not clear as to whether the fund in question was perpetual or terminable and also that it was not clear as to how the liability for the loss of the respondent society can be fastened on the said fund. The sub-committee recommended an amendment of the bye-law 50 and pursuant to this recommendation, at a general meeting of the respondent held on June 30, 1965, bye-law 50 was amended to run as follows :

> There shall be established a Loss Equalisation and Capital Redemption Reserve Fund in the Society. Every producer shareholder shall deposit every year a sum not less than 32 paise and not more than 48 paise per quintal of the sugarcane supplied by him to the society as may be determined by the Board, until the shares to be subscribed by a member are fully paid up. The amounts standing to the credit of this fund presently or to be credited on future shall be used for making the partly paid shares fully paid up. The balance of the said account shall be refunded to the members concerned soon after the present loan from the Industrial Finance Corporation of India is repaid, whereafter the fund shall cease to exist.

This amended bye-law shall be deemed to have come into force from July 1, 1958.

4. It may be mentioned here that the respondent society came into existence in 1958-59 and the original bye-laws came into force from July 1, 1958. The Income-tax Officer in assessing the respondent for the relevant assessment year held that the said sum of Rs. 5,15,863 represented a revenue receipt and was liable to be included in the taxable income of the assessee. On appeal the Appellate Assistant Commissioner affirmed the view of the Income Tax Officer holding that the case has to be decided on the basis of the bye-law as it stood during the relevant accounting year. The respondent assessee went in appeal to the Income Tax Appellate Tribunal which took the view that the amended bye-law 50 must be held to be operative even during the relevant previous year in view of the retrospective amendment thereof and that in view of the said amendment bye-law 50 the deposits made by the members by way of deductions from the price as contemplated in bye-law 50 were in the nature of permanent liabilities and hence they were capital receipts and not liable to be included in the taxable income of the respondent assessee. The Tribunal allowed the appeal of the assessee and directed that the said amount of Rs. 5,15,863 should be deducted from the taxable income of the assessee as determined by the Income Tax Officer. At the instance of the Commissioner a reference was made to the Allahabad High Court and the question framed for determination of the High Court was as follows :

Whether on the facts and in the circumstances of the case, the Income Tax Appellate Tribunal was right in holding that the amount of Rs. 5,15,863 was not a revenue receipt liable to tax ?

5. The Division Bench of the High Court which disposed of the said reference agreed with the view of the Tribunal that the bye-law 50 of the bye-law of the society was validly amended with retrospective effect and that retrospective effect must be given to that bye-law. The Division Bench took the view that in view of the amended bye-law the amount of Rs. 5,15,863 was not an amount which the society could deal with as its income or according to its will and hence the source of the receipt was diverted. The High Court answered the question referred to it in affirmative and in favour of the assessee. The present appeal is directed against the said decision of the High Court.

6. Before coming to the contentions urged by the respective counsel, it will be useful to take note of the relevant statutory provisions and the relevant rules. The respondent society was registered under the Co-operative Societies Act of 1912. Clause (a) of Section 2 of the said Act of 1912 defines "bye-laws" as registered bye-laws for the time being in force and includes a registered amendment of the bye-laws. Section 6 deals with the conditions for the registration of a co-operative society. Section 43 confers upon the State Government power to make rules for registered societies to carry out the purposes of the said Act. The relevant portion of clause (c) of sub-section (2) of Section 43 runs as follows :

> 43(2) In particular and without prejudice to the generality of the foregoing power, such rules may -
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> (c) prescribe the matters in respect of which a society may or shall make bye-laws, and for the procedure to be followed in making, altering and abrogating bye-laws, and the conditions to be satisfied prior to such making, alteration or abrogation;

7. Clause (e) of Section 43(2) runs as follows :

> In particular and without prejudice to the generality of the forgoing power, such rules may -
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> (e) regulate the manner in which funds may be raised by means of shares of debentures or otherwise;

8. Pursuant to the powers conferred under Section 43 of the U. P. Co-operative Societies Act, 1912, the Government of U. P. framed certain rules known as United Provinces Co-operative Societies Rules, 1936 for registered societies and these rules were in force at the relevant time. The relevant portion of Rule 8 under heading "III Bye-laws" ran as follows :

> A society shall, subject to the provisions of the Act and of the rules, make bye-laws in respect of the following matters, namely :-
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> (1) the name of society;
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> (2) its registered address;
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> (3) its aims and objects;
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> (4) the purposes for which its funds may be applied;

9. Rule 10 conferred power on a society to make bye-laws in respect of any other matter incidental to the management of its business. Rule 11 which deals with the amendment of rules runs as follows :

> An amendment may be made in the bye-laws, i.e. a bye-law may be altered or rescinded or a new bye-law added by a resolution passed by the votes of at least two-thirds of the members present at a special meeting called for the purpose.

10. It was submitted by Mr Ahuja, learned counsel for the appellant (revenue) that the amendment of bye-law 50, although it was purported to be made with retrospective effect could, in fact, have no

retrospective effect in law. It was submitted by him that a co-operative society governed by the Co-operative Societies Act, 1912 was not a body constituted by the said Act nor a statutory body. The power to make bye-laws was conferred upon the society by delegation under rules which themselves were framed by the government in exercise of power delegated to the government by the legislature under Section 43 of the aforesaid Act of 1912. It was submitted by him that as there was no delegation of any power on the respondent society to make bye-laws with retrospective effect, it had no power to do so and the amendment of bye-law 50 made by the society, although purporting to be retrospective, could not be given any such effect. In support of this submission, Mr Ahuja relied upon the decision of this court in ITO v. M. C. Ponnoose [(1969) 2 SCC 351 : (1970) 1 SCR 678 : (1970) 75 ITR 174], in which the court held as follows : (SCC pp. 354-55, para 5)

> Where any rule or regulation is made by any person or authority to whom such powers have been delegated by the legislature it may or may not be possible to make the same so as to give retrospective operation. It will depend on the language employed in the statutory provision which may in express terms or by necessary implication empower the authority concerned to make a rule or regulation with retrospective effect. But where no such language is to be found it has been held by the courts that the persons or authority exercising subordinate legislative functions cannot make a rule, regulation or bye-law which can operate with retrospective effect (See Subba Rao, J, in Dr Indramani Pyarelal Gupta v. W. R. Nathu [(1963) 1 SCR 721 : AIR 1963 SC 274], the majority not having expressed any different opinion on the point; Modi Food Products Ltd. v. CST [AIR 1956 All 35 : 6 STC 287],; India Sugar Refineries Ltd. v. State of Mysore [AIR 1960 Mys 326], and General S. Shivdev Singh v. State of Punjab [(1959) 61 Punj LR 514 (Punj HC) (FB) : AIR 1959 Punj 453]

11. The aforesaid observations have been cited with approval by this Court in Hukam Chand v. Union of India [(1972) 2 SCC 601 : (1973) 1 SCR 896 : AIR 1972 SC 2427], where the Central Government was held to have acted in excess of its powers insofar as it gave retrospective effect to the Explanation to Rule 49 framed under the Displaced Persons (Compensation and Rehabilitation) Act, 1954, exercising the powers conferred by Section 40 of the Act. We may also refer here to the decision of this Court in Co-operative Central Bank Ltd. v. Additional Industrial Tribunal, Andhra Pradesh [(1969) 2 SCC 43 : (1970) 1 SCR 205 : (1970) 40 Com Cas 206], where it has been stated by this Court as follows : (SCC p. 53, para 10)

> We are unable to accept the submission that the bye-laws of a co-operative society framed in pursuance of the provisions of the Act can be held to be law or to have the force of law. It has not doubt been held that, if a statute gives power to a government or other authority to make rules, the rules so framed have the force of statute and are to be deemed to be incorporated as a part of the statute. That principle, however, does not apply to bye-laws of the nature that a co-operative society is empowered by the Act to make. The bye-laws that are contemplated by the Act can be merely those which govern the internal management, business or administration of a society.

12. We may mention that the Act under which the Bye-laws were framed was the Andhra Pradesh Co-operative Societies Act, 1964.

13. In the light of the decisions discussed earlier, it appears to us that the respondent society had no authority in law to amend bye-law 50 with retrospective effect as it purported to do. We have

already pointed out the power of the society to amend its bye-laws arises from the provisions of Rule 11 of the United Provinces Co-operative Societies Rules, 1936, which rule has been made under the powers conferred by Section 43 of the United Provinces Co-operative Societies Act 1912. There is nothing expressly or impliedly in Rule 11 which confers any power on the society to amend its bye-laws with retrospective effect and in the absence of any such power being conferred, either expressly or by implication, it cannot be said that the society had any power to amend its bye-laws with retrospective effect. Mr Manchanda, learned counsel for the respondent-society placed strong reliance on the decision of this Court in Dr Indramani Pyarelal Gupta v. W. R. Nathu [(1963) 1 SCR 721 : AIR 1963 SC 274], where it was held that the substituted bye-law 52-AA of the East India Cotton Association made by the Central Government in exercise of the power conferred upon it under Section 12 of the Forward Contracts (Regulation) Act, 1952 and which, very shortly stated, conferred power on the Forward Markets Commission, after notifying with the Chairman of the Board of the East India Cotton Association, to close hedge contracts in the eventualities mentioned in the said rule was not invalid in law or ultra vires the Constitution. On a proper construction, the amended or substituted bye-law applied not only to contracts to be entered into in future but also to subsisting contracts. This Court pointed out that, in that case, the power to make bye-laws so as to affect that the rights in subsisting contracts followed as necessary implication from the terms of Section 11 of the Forward Contracts (Regulation) Act, 1952. In the case before us, however, there is nothing in Section 43 of the U. P. Co-operative Societies Act, 1912 or Rule 11 of the United Provinces Co-operative Societies Rules, 1936 to indicate that there is any power, express or implied, in a co-operative society registered under that Act to make bye-laws with retrospective effect in respect of its business.

14. In view of the above discussion, in our view, the amendment of bye-law 50 of the respondent society cannot have any retrospective effect and the amounts deducted from the amounts payable to members for the supply of sugarcane, will have to be dealt with as if they were deducted under the provisions of bye-law 50 as it stood in the relevant accounting period.

15. If the provisions of the unamended bye-law are to be applied, it is clear that these amounts which were deducted by the respondent from the price payable to its members on account of supply of sugarcane were deducted in the course of the trading operations of the respondent and these deductions were a part of its trading operations. The receipts by way of these deductions must, therefore, be regarded as revenue receipts and are liable to be included in the taxable income of the respondent. It is urged by Mr Manchanda, that these receipts have been described in the bye-law 50 as deposits, but we fail to see how they can really be regarded as deposits. It was held by this Court in Chowringhee Sales Bureau P. Ltd. v. C. I. T. [(1973) 1 SCC 46 : (1973) 87 ITR 542 : 1973 SCC (Tax) 163 : (1973) 31 STC 254], that it is the true nature and quality of the receipt and not the head under which it is entered in the account books as would prove decisive. If a receipt is a trading receipt, the fact that it is not so shown in the account books of the assessee would not prevent the assessing authority from treating it as a trading receipt. The same principle can be derived from the decision of this Court in Punjab Distilling Industries Ltd. v. CIT [(1959) 35 ITR 519 : AIR 1959 SC 346 : ILR 1959 Punj 656]. In that case, the assessee carried on business as a distiller of country liquor and sold the produce of its distillery to licensed wholesalers. Under a scheme devised by the government, the distiller (assessee) was entitled to charge the wholesaler a price for the bottles in which the liquor was supplied, at rates fixed by the government, which he was bound to repay when the bottles were returned. In addition to the price fixed under the government scheme, the assessee took from the wholesalers certain further amounts, described as security deposits without the government's sanction and entirely as a condition imposed by the assessee itself for the sale of its liquor. The moneys described as security deposits were also returned as and when the bottles were

returned but in this case the entire sum taken in one transaction was refused when 90 per cent of the bottles covered by it were returned. The price of the bottles received by the assessee was entered by it in its general trading account while the additional sum was entered in the general ledger under the heading "empty bottles return security deposit account". The question was whether the assessee could be assessed to tax on the balance of the amounts of these additional sums left after the refunds made out of the same. It was held that the additional amount described as security deposit by the assessee was really an extra price for the bottles and was part of the consideration for the sale of liquor; it did not make any difference that the additional amount was entered in a separate ledger termed "empty bottles return deposit account". It was held that these additional amounts, which remained after the refunds were made, were trading receipts of the assessee and liable to tax. Applying these principles to the present case, in our opinion, it makes no difference that in the bye-law, these amounts have been referred to as deposits and the account in which these receipts were entered has been called "Loss Equalisation and Capital Redemption Reserve Fund". The essence of a deposit is that there must be a liability to return it to the party by whom or on whose behalf it is made on the fulfillment of certain conditions. Under the amended (sic unamended) bye-law, the amounts deducted from the price and credited to the said fund were first liable to be used in adjusting the losses of the respondent society in the working year; thereafter in the repayment of initial loan from the Industrial Finance Corporation of India and then for redeeming the governments share and only in the event of any balance being left, it was liable to be converted to share capital. The primary purpose for which the deposits were liable to be used were not to issue shares to the members from whose amounts the deductions were made but for the discharging of liabilities of the respondent-society., In these circumstances, the receipts constituted by these deductions were really trading receipts of the assessee society and are liable to be included in its taxable income. In our view, the learned judges of the High Court were, with respect, in error in answering the question refereed in the negative. In our opinion, the question referred must be answered in affirmative and in favour of the revenue.

16. In the result, the appeal succeeds and is allowed with costs. The respondent shall also pay to the appellant the costs incurred in Income Tax Reference No. 67 of 1979.

Civil Appeal No. 564 of 1975

17. This is an appeal against the judgment of a Division Bench of the Allahabad High Court in Income Tax Reference No. 724 of 1971. The question referred to us for determinations is as follows :

> Whether on the facts and in the circumstances of the case, the sum of Rs. 6,11,846 credited during the year of account to the loss equalisation and capital redemption reserve fund by deposits received from producer members of the society under Clause 50 of its bye-laws is of revenue nature assessable to tax ?

18. In view of our decision, the appeal must be allowed and the question referred answered in the affirmative and in favour of the revenue. The appeal is allowed. No order as to costs.

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