KERALA HIGH COURT

Helen Rubber Industries Ltd

Vs.

Commissioner of Income-tax

Income-tax Ref. No. 2 of 1956

(Kumara Pillai and T.K. Joseph, JJ.)

31.10.1958

JUDGMENT

Kumara Pillai, J.

1. This is a reference made by the Madras Bench of the Income-tax Appellate Tribunal under Section 66(2) of the Indian Income-tax Act in compliance with the direction of the High Court of Travencore-Cochin State in the order in Original Petition No 194 of 1955.

2. The assessee, Helen Rubber Industries Limited is a company incorporated in the former State of Travencore and having its registered office at Kottayam. It had a factory for the manufacture of rubber goods at Kottayam (not at Kanjirappally as wrongly stated in the order of reference by the Income-tax Appellate Tribunal). In the Malabar year 1116 the assessee-company (referred to hereinafter as the company) leased the aforesaid factory for a period of 15 years to certain persons (referred to hereinafter as lessees) by a registered instrument. Clauses 14 and 16 of the lease-deed provide for payment of damages in certain circumstances by the lessees to the company. They read :

> "14, The lessees further covenant and guarantee that during the continuance of the lease and for a period of three years after the expiration of the lease, the lessees or any of them shall not directly or indirectly work for, advise or be in any manner connected with any other rubber goods manufacturing concern or themselves carry on any such concern except continuing the business of manufacturing goods from Rubber latex now carried on by them at Kanjirappally and that on the breach of any of the above guarantees the lessees shall pay the lessors a lump sum of Rs. 10,000 only as compensation therefor."

16. "If the lessees discontinue the lease before the efflux of the period herein provided or cause such discontinuance by their default to observe or by their breach of any of the terms of this agreement to be observed or performed by them, the lessees shall become liable and shall pay to the lessors a sum of Rs. 10,000 by way of liquidated damages for such discontinuance ....."

Disputes and dissensions arose between the lessees and the company shortly after the grant of the-lease, and these disputes and dissensions gave rise to four suits between them in the District Court of Kottayam; (1) O.S. No. 134 of 1117 and (2) O.S. No. 126 of 1121 instituted by the lessees against the company and another person : and (3) O.S. No. 144 of 1118 and (4) O.S. No. 180 of 1124 instituted by the company against the lessees. All those disputes and suits were finally settled by a compromise by which the lease was terminated. Under the compromise the lessees also paid to the company a sum of Rs. 23,311-3-0 on account of the damages provided for in Clauses 14 and 16 of the lease deed and certain other claims, and it was credited in the company's accounts as follows :

Balance due on ledger account	Rs. 8,186 0 0
Damages for breach of clause 14 of the lease deed	" 7,075 1 6
Damages for breach of clause 16 of the lease deed	" 8,050 1 6
	" 23,311 3 0

3. This payment was made after the extension of the Indian Income-tax Act to Travencore-Cochin by the Indian Finance Act, 1950. The first assessment on the company under the Indian Income-tax Act was for the year 1950-51, accounting period : 1949 A.D. Before that, the company was being assessed under the Travencore Income-tax Act, 1121, and in respect of the three assessments prior to the assessment of 1950-51 namely, the assessments for the Malabar years 1123, 1124 and 1125-the company was not taxed at all as it had made no profits during the relevant accounting periods and had incurred only losses. In 1950-51 also the company was not taxed as it had no profits or gains during the accounting period, and it was expressly stated in the assessment order of that year that the losses of 1123, 1124, 1125 M.E. and 1950-51, A.D., amounting in all to Rs. 14,003-1-3, were to be carried forward. That assessment order says :

> "The assessee has returned a loss of Rs. 3,954/-. Sri Cherian, company's auditor representative appeared with the accounts in response to this office notice under Section 23(2). They were examined. The taxable income is fixed as under :

Loss as per Profit and Loss statement filed :	Rs. 1908-12-0
Deduct inadmissible items like presents etc.	Rs. 21-4-0
Net loss	Rs. 1887-8-0

The company has claimed depreciation for furniture, machinery, etc., but the factory was not working during the accounting period. Hence no depreciation can be allowed. Net adjusted loss for 1950-51 .... Rs. 1887-8-0

Add loss of 1123 carried over

	Rs. 4031-10-0
1124.....	5479-1-0
1125.....	2604-13-0
	12115-9-3
Total	Rs. 14003-1-3

This will be carried forward."

4. The accounting period for the next assessment, namely the assessment for 1951-52 was the year 1950. In making the return for that assessment the company again showed a net loss. The Income-tax Officer refused to accept this return as correct Out of the sum of Rs. 23311-3-0 which the company had received in 1950 under the compromise with the lessees, it had credited in its accounts Rs. 15125-3-0 as damages for breach of Clauses 14 and 16 of the lease deed, Rs. 7075-1-6 as damages for breach of Clause 14 and Rs. 8050-1-6 as damages for breach of Clause 16. The Income-tax Officer treated this amount of Rs. 15125-3-0 as an item of profit or gain liable to tax, and adding that amount to the gross receipts of the company and deducting from the grand total other expenses and allowances which he considered to be permissible, he held that the company had made a net gain of Rs. 502/- during the accounting period and assessed it to income-tax on the said amount of Rs. 502/-. Although in the assessment order of 1950-51 which was made under the Indian Income-tax Act it was expressly stated that the losses of 1123, 1124, 1125 M.E. and 1950-51 A.D., amounting in all to Rs. 14,003-1-3, "will be carried forward" in making the assessment for 1951-52 the Income-tax Officer allowed deductions only in respect of the losses of 1124, 1125 M.E. and 1950-51 A.D. and disallowed the loss of 1123 M.E. amounting to Rs. 4031-10-0 on the ground that it had lapsed.

5. Against this assessment the company preferred an appeal to the Appellate Assistant Commissioner of Income-tax Trivandrum complaining that the loss of 1123 M.E. also should have been taken into account and a deduction or set off allowed in respect of it in making the assessment for I1951-52 and that the amount of Rs. 15,125-3-0 credited in their accounts as damages received from the lessees for breach of Clauses 14 and 16 of the lease deed was not an item of profit or gain from the business liable to tax but only a capital or casual receipt exempt from tax. The Appellate Assistant Commissioner dismissed the appeal by a very brief order in which he observed as regards the contention for deduction or set off of the loss of 1123 M.E. :

> "The Income-tax Officer refused this set off since the loss 'lapsed' prior to the year of account itself under Section 32 of the Travencore Income-tax Act, 1121. I have therefore no ground to interfere with this refusal."

and as regards the contention that the amount of Rs. 15,125-3-0 was not liable to tax :

> "The Income-tax Officer has given convincing reason in the assessment order for treating the said amount as income liable to tax "and I am in full agreement with him in his conclusion. I therefore regret my inability to give any relief to the appellant under thus head either."

6. Against the Appellate Assistant Commissioner's order the company preferred an appeal to the Income-tax Appellate Tribunal, I.T.A. No. 8165/53-54, which was heard and disposed of by the Madras Bench 'A' of the Appellate Tribunal, on 11-10-1954. That appeal also was dismissed, and then the company applied for a reference to the High Court under Section 66(1) of the Indian Income-tax Act. The Tribunal refused to make a reference on the ground that the case involved only questions of fact and not questions of law. Thereupon the company filed original petition

No. 194 of 1955 in the High Court of Travencore-Cochin for compelling the Tribunal to make a reference under Section 66(2) of the Indian Income-tax Act, and on 2-2-1956 the High Court allowed that original petition and directed the Tribunal to make a reference. This reference has been made accordingly, and the questions referred are :

> "(i) Whether under the provisions of the Indian Income-tax Act the petitioner is entitled to carry forward the loss for a period of six years notwithstanding the fact that during the period when the loss had occurred the law applicable was the Travencore Income-tax Act; and
> (ii) Whether the amount of Rs. 15125-3-0 received by the petitioner from the lessee of the factory is assessable or not ?"

7. Question No. 1 relates to the company's complaint as regards the omission to give relief to it in respect of the loss of 1123 M.E. by setting off that loss against the profits and gains made during the accounting period for the assessment of 1951-52. Originally there was no provision in the Travencore income-tax Act for carrying forward losses of previous years and setting them off against the profits or gain of subsequent years. The provision in this behalf was made for the first time by the amended Act of 1121 which came into force on the first day of 1122 M.E. and is contained in Section 32(2). Under that section losses of years subsequent to 1126 M.E. can be carried forward for six years, and different periods are prescribed for carrying forward losses of the years 1122 to 1126 M.E. Losses of 1122 can be carried forward for only one year, 1123 for two years, 1124 for three years, 1125 for four years and 1126 for five years. In the Indian Income-tax Act provision in this behalf is made in Section 24(2). That section, as it stood at the time of the assessment of 1951-52, provided that losses of years subsequent to the 31st March 1944 could be carried forward for six years and prescribed a sliding arrangement for carrying forward the losses of the years ending 31st March 1940, 31st March 11941, 31st March 1942, 31st March 1943 and 31st March 1944, similar to the arrangement in Section 32(2) of the Travencore Act, for carrying forward the losses of the years 1122 to 1126. The loss of the year ending 31st March 1940 was to be carried forward for only one year, and the loss of the year ending 31st March 1944 was to be carried forward for five years; and the losses of the other three years were to be earned forward for two, three and four years respectively. The Malabar year 1123 commenced on 17-8-1947 and ended on 17-8-1948, and was within six years of the assessment year 1950-51. The company would, therefore, be entitled, under Section 24(2) of the Indian Income-tax Act to carry forward and set off the loss of 1123 against the profits and gains of 1951-52 if there were no profits or sufficient profits in 1123 M.E. and the years prior to 1951-52 for setting off such loss. Under Section 32(2) of the Travencore Act, the loss of 1123 could be carried forward for this purpose only for two years and could not be taken into account in making the assessments for the years subsequent to that period, that is to say, the loss of 1123 M.E. cannot be set off against the prompts of the assessment years subsequent to 1125 M.E. As the assessment of 1951-52 is for a period subsequent to 1125 M.E. (the corresponding dates according to the Malabar Era for 1-4-1951 and 31-3-1952 are 18-8-1126 and 18-8-1127), the company would not be entitled under Section 32(2) of the Travencore Income-tax Act to carry forward the loss of 1123 and set it off against the profits and gains of 1951-52 for the purposes of the assessment of that year. The company's case is that, as the assessment for 1951-52 was made under the Indian Income-tax Act, the set off of the losses of the previous years has to be made under Section 24(2) of the Indian Act and not under Section 32(2) of the Travencore Act find

that, therefore, for the purpose of the assessment of 1951-52 it was entitled to have the loss of 1123 taken into account and set off against the profits of 1951-52. The Appellate Tribunal overruled this contention saying :

> "The carry forward of losses has to be determined under the law as it existed at the time when the loss occurred, which in this case is in 1123 M.E., and this had admittedly lapsed by 1125 M.E., long before the Indian Income-tax Act was ever thought of being applied to these territories and as such, the department has rightly declined to carry forward the loss which had already lapsed.

Whether this statement of the law by the Appellate Tribunal is correct, and whether an assessee who was being assessed under the Travencore Income-tax Act till the extension of the Indian Income-tax Act to Travencore-Cochin, continues to be governed by Section 32(2) of the Travencore Act or will be governed by Section 24(2) of the Indian Act as regards the carry forward of the losses of previous years and their set off for purposes of assessments guide in respect of periods subsequent to the extension of the Indian Act, are the main points for consideration so far as question No. 1 is concerned.

8. It is now well settled that when there has been a change or amendment of law, the assessment has to be made in the absence of an express provision to the contrary according to the law as it is at the time of the assessment, i.e., according to the law as it is in the year of assessment, and not according to the law as it was at the time of the income, profit or gain sought to be assessed was earned. We shall refer to a few cases in which this question has come up for consideration. In the *Commissioner of Income-tax, Bombay v. Sind Hindu Provident Funds Society*[1], the Chief Court of Sind had to consider the effect of a change in the rules regarding exemption from tax of interest on Government securities. The assessment in that case was for the year 3 936-37 and was made on the income derived by the assessee in 1935-36. On the strength of a Government notification of the 31st March 1923 the assessee claimed exemption from tax on the entire interest, amounting to Rs. 67,040/- he had received on Government securities purchased through the post office and held in the custody of the Accountant General, Posts and Telegraphs. The Income-tax Authorities disallowed the claim for exempting the entire interest and allowed exemption only in respect of a sum of Rs. 22,500/- out of the amount of Rs. 67,040 on the ground that another Government notification of 1936 had prescribed the maximum limit of exemptions in such cases at Rs. 22,300. The assessee contended that, as the assessment for 1936-37 was made on the income of 1935-36, the Government notification of 1936 would not apply to the assessment and that he was entitled to get the entire amount of Rs. 67,040 received as interest exempted from tax under the Government notification of 1922, and took up the case, by way of a reference, to the Chief Court. During the course of the arguments in the Chief Court it transpired that there was- another notification of the 2nd November 1935 also prescribing the same

[1](1940) 8 ITR 467 : AIR 1941 Sind 110

maximum limit, i.e., Rs. 22,500 for such exemptions. In repelling the assessee's contention, after mentioning the fact that besides the notification of 1936 there was also the earlier notification of 2nd November 1935, Davis, C.J., observed in his judgment;

> "..... But we do not think that if there had been no notification of 1935 but only the notification of 1936, that would have helped the assessees at all, because while it is true

that the quantum of the income for the assessment of the year 1936-37, was the income of the year 1935-36 the assessment was not for the year 1935-36, but for the year 1936-37, and it appears to us that the law and statutory rules applicable for determining the assessment must be statutory law and rules in force in the year of the assessment, i.e., in 1936-37, when the assessees would clearly be entitled only to the limited exemption of Rs. 22,500/- in our view even if there had been no notification of 1935 the question raised in the reference would have been decided against him."

9. The Madras High Court also has held in *Commissioner of Income-tax, Madras v. Maharaja of Pithapuram*[2], that it is the law in force at the time of the assessment which governs the assessment and not the law as it was during the year in which the income was earned. This decision was affirmed in appeal by the Privy Council in *Maharaja of Pithapuram v. Commissioner of Income-tax, Madras*[3], The case related to an assessment of the year 1939-40 made on the income of the year 1938-39. In 1933 the assessee had executed certain revocable instruments of trusts, and settlements in favour of his four daughters; and, up to the assessment in question, the income which the daughters derived from the assets transferred to them under those instruments was being treated as their separate income and the assessee was not being taxed in respect of such income. But the Indian Income-tax Amendment Act 7 of 1939, which came into force on the 1st April 1939, contained a provision that

> "all income arising to any person by virtue of a revocable transfer of assets shall be deemed to be income of the transferor"

and on account of this amendment in law the Income-tax Officer included in the assessee's assessment for 1939-40 the income derived in 1938-39 from the assets transferred to his daughters under the revocable instruments. The assessee contended that, as the tax was being levied on the income of 1938-39 the provision in the Amendment Act of 1939, which came into force only on the 1st April, 1939, would not apply to the assessment. His contention was not accepted by the Income-tax authorities, and on reference being made to the Madras High Court, a Full Bench of that court also repelled the contention holding that the law in force at the time of the assessment must govern the assessment and not the law in the previous year in which the income was earned and that as the amendment Act had come into force on the 1st April, 1939 the assessment of 1939-40 had to be made according to the provisions of the amendment Act (see (1942) 10 ITR 1 : AIR 1942 Madras 191). Against the decision of the High Court the assessee preferred an appeal to the Privy Council. The Privy Council also overruled the assessee's contention saying :

[2](1942) 10 ITR 1 : (AIR 1942 Mad191)

[3](1945) 13 ITR 221 : (AIR 1945 PC 89)

> "..... In the first place, it is clear to their Lordships that under the express, terms of Section 3 of the Indian Income-tax Act, 1922, the subject of charge is not the income of the year of assessment, but the income of the previous year. This is in direct contrast to the English Income-tax Acts, under which the subject of assessment is the income of the year of assessment, though the amount is measured by a yardstick based on previous years, The difference is well illustrated by the distinction that in England the source of income must still be extant in the year of assessment but that that is not of relevance in

> India. Their Lordships may refer to the able judgment of Rankin, C.J., in Behari Lal Mullick, in the matter of ILR 54 Cal 630 : 2 ITC 328 : AIR 1927 Calcutta 553, with which they agree.
>
> "In the second place, it should be remembered -that the Indian Income-tax Act, 1922, as amended from time to time, forms a code, which has no operative effect except so far as it is rendered applicable for the recovery of tax imposed for a particular fiscal year by a Finance Act. This may be illustrated by pointing out that there was no charge on the 1938-39 income either of the appellant or his daughters, nor assessment of such income, until the passing of the Indian Finance Act of 1939, which imposed the tax for 1939-40 on the 1938-39 income and authorized the present assessment.

By Sub-Section (1) of Section 6 of the Indian Finance Act, 1939, income-tax for the year beginning on the 1st April, 1939 is directed to be charged at the rates specified in Part I of Schedule II, and rates of super-tax are also provided for, and by Sub-Section (3) it is provided that 'for the purpose of this section and of Schedule II the expression 'total income' means total income as determined for the purposes of the Indian Income-tax Act, 1922. This can only refer to the Indian Income-tax Act, 1922, as it stood amended at the date of the Indian Finance Act, 1939, and necessarily includes the alterations made by the amending Act, which had already come into force on the 1st April, 1939."

10. This Privy Council decision was followed by the Allahabad High Court in In re, Mishrimal Gulabchand of Beawar, (1950) 18 ITR 75 : AIR 1950 Allahabad 270, and by the Nagpur High Court in *Commissioner of Income-tax v. C.P. Syndicate*[4], In both these cases it was held that as Section 14(1) of the Indian Income-tax Act came into force only on the 11th April, 1944 the assessments for the year 1944-45 will not be governed by that section and that the assessments for those years must be governed by the law in force on the 1st April, 1944.

11. The carry forward of losses of previous years and their set off against the profits and income of the assessment year is only a process for arriving at or fixing the assessable income and is a part of the assessment itself. Therefore the principle of the decisions in the cases mentioned above must ordinarily apply to the carry forward of the losses and their set off, and we are unable to accept as correct the statement of law in the order of the Income-tax Appellate Tribunal that the

> "carry forward of losses has to be determined under the law as it existed at the time when the loss occurred."

[4](1952) 22 ITR 493 : (AIR 1953 Nag 77)

As the assessment has to be made according to the law as it is in the year of assessment, and not as it was at the time the profits or income sought to be assessed accrued, the carry forward of losses of previous years and their set off against the profits and income of the assessment years also has to be determined, in the absence of any express provision to the contrary, according to the law as it is in the assessment year and not as it was at the time the losses occurred.

12. The Indian Income-tax Act was extended to Travencore-Cochin and the Travencore Income-tax Act was repealed by Sections 3 and 13 of the Indian Finance Act of 1950. Section 13(1) of

the Finance-Act of 1950 provides :

> "13. (1) If immediately before the 1st day of April, 1950, there is in force in any Pant B State other than Jammu and Kashmir or in Manipur Tripura or Vindhya Pradesh or in the merged territory of Cooch-Behar any law relating to income-tax or super-tax or tax on profits of business, that law shall cease to have effect except for the purposes of the levy, assessment and collection of income tax and super-tax in respect of any period not included in the previous year for the purposes of assessment under the Indian Income-tax Act, 1922. (XI of 1922) for the year ending on the 31st day of March, 1951, or for any subsequent year, or, as the case may be, the levy, assessment and collection of the tax on profits of business for any chargeable accounting period ending on or before the 31st day of March, 1949."

Because of this extension of the Indian Income-tax Act and repeal of the Travencore Income-tax-Act the assessments on the company for 1950-51 and 1951-52 were made under the Indian Act and not under the Travencore Act. Necessarily therefore, the carry forward of the losses of previous, years and their set off against the profits and income of the assessment year 1951-52 and subsequent years will be governed by Section 24(2) of the Indian Income-tax Act if there is no express provision of law excluding the operation of that section. According to the learned counsel for the income-tax department, so far as the assessees who were being assessed under the former State laws fill the extension of the Indian Income-tax Act to Part B States are concerned, Section 3 of the Taxation Laws (Part B States) (Removal of Difficulties) Order 1950, has expressly curtailed the rights which they would otherwise have had under Section 24(2) of the Indian Income-tax Act. He contended that that section limits the rights of those assessees to carry forward the losses of previous years to periods during which they could have carried forward the particular losses under the law in existence before the extension of the Indian Income-tax Act (in this case, under the Travencore Income-tax Act) and that in view of it the Company's loss of 1123 could be carried forward only for two years, as that was the period during which it could be carried forward under Section 32(2) of the Travencore Income-tax Act.

Section 3 of the Taxation Laws (Part B States) (Removal of Difficulties) Order, 1950, has not been noticed by the Appellate Tribunal or the Appellate Assistant Commissioner. It was only at the time-of hearing in this court that that section was sought to be relied upon in support of the department's case that the loss of a previous year which would not have been available to an assessee under the repealed law of the former State to be carried forward to the particular assessment year, could not be carried forward and set off in the assessment year even though it was permissible under the Indian Income-tax Act to carry it forward to that assessment and make the set off. In answer to this contention based on Section 3 of the Taxation Laws (Part B States) (Removal of Difficulties) Order, 1950, it was contended on behalf half of the company that the construction put upon that section by the learned counsel for the department is wrong. According to the company's learned counsel, Section 3 of the Taxation Laws (Part B States) (Removal of Difficulties) Order, 1950, was enacted for the purpose of securing to the assessees newly brought under the Indian Income-tax Act such larger right as would have been available to them under the provisions of the repealed State laws, corresponding to Section 24(2) of the Indian Income-tax Act if the State laws had continued to be in force and had not been superseded by the Indian Income-tax Act. His contention was that Section 3 of the Taxation Laws (Part B States)

(Removal of Difficulties) Order, 1950, does not curtail1, but enlarges, so far as these new assessees are concerned, the rights under Section 24(2) of the Indian Act.

13. In our opinion the contention of the company's learned counsel is sound and has to be accepted. The power given by Section 12 of the Finance Act, 1950, to the Central Government is to make orders for removing any difficulty which arises in giving effect to the provisions of the Acts extended to the Fart B States or merged territories by Section 3 or Section 11 of that Act. So far as the Income-tax Department is concerned, there can be no difficulty at all in giving effect to Section 24(2) of the Indian Income-tax Act, for in making the assessment for any particular year after the extension of the Indian Act the Income-tax Officer has only to deduct the losses sustained by the assessee during the period allowable under Section 24(2) from the income of the assessment year and fix the assessable income. But, to the assessees newly brought under the Indian Income-tax Act there would be real difficulty in the application of Section 24(2) to them if, under the State laws to which they were subject till the extension of the Indian Act, they were entitled to larger rights than under Section 24(2) of the Indian Income-tax Act as to the manner and set off of losses. The right of carry forward and set off given by Section 24(2) of the Indian Income-tax Act is hedged in by very important limitations. Section 24, sub-clauses (2A) and (2B), read as follows :

> "(2-A) Notwithstanding anything contained in Sub-Section (1) where the loss sustained is a loss falling under the head 'Capital gains', such loss shall not be set off except against any profits and gains falling under that head."
> "(2-B). Where an assessee sustains a loss such as is referred in to Sub-Section (2-A) and the loss cannot be wholly set off in accordance with the provisions of that Sub-Section, the portion not so set off shall be carried forward to the following year and set off against capital gains for that year, and if it cannot be so set off the amount thereof not so set off shall be carried forward to the following year and so on, so however, that no such loss shall be so carried forward for more than six years :
> Provided that where the loss sustained in any previous year does not exceed fifteen thousand rupees, it shall not be carried forward."

Sub-clause (2-A) is a limitation on the right conferred on assessees by Section 24(1), and sub-clause (2-B) and the proviso thereto are two limitations en the right conferred by Section 24(2). Although, under Section 24(2), the assessee will be entitled to carry forward all kinds of losses of profits and gains incurred in a previous year under the head "profits and gains of business, profession or vocation" and set off the same against all the income from, the profits and gains of the same business, profession or vocation in a subsequent year during the period of six years, the effect of sub-clause (2-B) would be that such part of the loss as would fall under the term "capital gains" (referred to hereinafter as capital loss) can be set off only against capital gains of the subsequent years and not against all the income under the head "profits and gains" of the same business, profession or vocation; and the effect of the proviso to Sub-Section (2-B) will be that even the right to carry forward "capital loss" of the previous year is available only when such losses exceed Rs. 15,000/-. There are no provisions in the Travencore Income-tax Act similar to Sections 24(2-A) and 24(2-B) and the proviso thereto in the Indian Income-tax Act and so, before the extension of the Indian Income-tax Act to Travencore-Cochin the assessees in

Travencore were entitled to carry forward "capital loss" of previous years even when such loss was below Rs. 15,000 and to set off the 'capital loss' against all the income in the subsequent year or years under the head 'profits and the gains of business, profession or vocation', subject, of course, to the restrictions as regards the period for which the losses of 1122, 1123, 1124, 1125 and 1126 could he carried forward under Section 32(2) of the Travencore Act. The effect of Section 3 of the Taxation Laws (Part B States) (Removal of Difficulties) Order, 1950, sol far as this larger right under Section 32(2) of the Travencore Income-tax Act is concerned is that even after the extension of the Indian Income-tax Act to Travencore-Cochin the assessees in Travencore who would have been entitled to carry forward the "capital loss" of 1123 or 1124 for two or three years (as the case may be) and set off the same against all the income under the head 'Profits and Gains' of the same business would continue to have that right during the period allowed by Section 32(1) of the Travencore Act despite the fact that under the Indian Act they would not be entitled to have that right; and they would also, be entitled to carry forward the 'capital loss' even if it was below Rs. 15,000/-. Section 3 of the Taxation Laws (Part B States) (Removal of Difficulties) Order, 1950, reads as follows :

> "3. Carry-forward and set off of previous losses : -
> " 'Where in any previous year" prior to the previous year for the assessment for the year ending on the 31st day of March, 1950, 'an assessee has sustained a loss of profits or gains' in any business, profession or vocation carried on by him, 'and such loss would', had the State law continued to be in force, 'have been set off against the profits and gains', if any, from the same business chargeable to tax in the said year of assessment or in any year subsequent thereto, 'such loss would be so set off in the same manner, to the same extent, and up to the same year of assessment, as it would have been set off had the State' law continued to be on force".

The words underlined (here in ' ') in the above extract would show how the section applies to cases of the above nature. If Section 3 of the Taxation Laws (Part B States) (Removal of Difficulties) Order, 1950, was not there the assessees newly brought under the. Indian Income-tax Act would be governed by Section 24(2) of the Indian Act, and the consequence would have been that all at once they would be deprived of the valuable right of carrying forward 'capital loss', even 'capital loss' below Rs. 15000 and have the same set off against all the income from the profits and gains of the same business in the subsequent years. Their right was saved by Section 3 of the Taxation Laws (Part B States) (Removal of Difficulties) Order, 1950; but in order to ensure that they could not have their right for the longer period of six years, during which losses other than 'capital loss' could be carried forward under Sections 24(2) and 24(2-B) to be set of against income other than capital gains, it was provided in Section 3 of the Taxation Laws (Pant B States) (Removal of Difficulties) Order, 1950, that the loss would be set off in the same manner, to the same extent, and up to the same year of assessment as it would have been set off had the State laws continued to be in force. In our opinion, it is to meet cases like this, and for curtailing the right which an assessee would get under Section 24(2) of the Indian Act upon the extension of that Act to Part B States, that Section 3 of the Taxation Laws (Part B States) (Removal of Difficulties) Order, 1950, has been enacted. If the intention in enacting this section was to curtail any larger rights which the assessees might get under Section 24(2) as a result of the extension of the Indian Act, the word 'only' or some such expression would undoubtedly have

been used before the expression 'in the same manner' occurring in the clause 'such loss would be so set off in the same manner, etc.', making that clause read : "such loss would be so set off only in the same manner, to the same extent, and up to the same year of assessment"; or some such similar expression would have been used to make the meaning clear that the section was intended to limit or curtail the rights under Section 24(2) of the Indian Income-tax Act. The result of the construction which the learned counsel for the department seeks to put upon Section 3 of the Taxation Laws (Part B States) (Removal of Difficulties) Order, 1950, would be to cause anomalies instead of removing difficulties. If that construction is accepted it would deny to the assessees in the States to which the Indian Income-tax Act was extended in 1950 the full benefits of Section 24(2) of the Indian Act while the assessees in the other States would continue to have all those benefits. In enacting Section 3 of the Taxation Laws (Part B States) (Removal of Difficulties) Order, 1950, it could never have been the intention to make this kind of discrimination against the assessees newly brought under the Indian Income-tax Act. As the extension was made for the purpose of securing uniformity Section 3 could have been intended only for the purpose of relieving temporary hardships which might be caused to the new assessees by the extension of the Indian Act and not for discriminating against them and depriving them of the rights under the newly extended Act. The anomaly which would result from accepting the construction contended for by the learned counsel for the department would not arise if the construction contended for by the company's counsel is the proper construction to be put upon Section 3 of the Taxation Laws (Part B States) (Removal of Difficulties) Order, 1950. These are important considerations to be kept in mind in construing Section 3.

14. The principles of construction in such cases have been stated as follows at page 17 of Maxwell's Interpretation of Statutes 1953, Edition :

> "It is an elementary rule that a thing which is within the letter of a statute will generally be construed as not within the statute unless it be also within the real intention of the legislature, and the words, if sufficiently flexible, must be construed in the sense which, if less correct grammatically, is more in harmony with that intention. "Where alternative constructions are equally open that alternative is to be chosen which will be consistent with the smooth working of the system which the statute purports to be regulating; and that alternative is to-be rejected which will introduce uncertainty, friction or confusion into the working of the system."

It is also pointed out, in the same page, that language is rarely so free from ambiguity as to be incapable of being used in more than one sense, and to adhere rigidly to its literal and primary meaning in all cases would be to miss its real meaning. The following observation of Maxwell at pages 18 and 19 of the same book are also worth quoting in this connection :

> "General words admit of indefinite extension or restriction, according to the subject to which they relate, and the scope and object in contemplation. They may convey faithfully enough all that was intended, and yet comprise also much that was not;.....The literal construction then, has, in general, but prima facie preference. To arrive at the real meaning, it is always necessary to get an exact conception of the aim, scope, and object of the whole Act; to consider according to Lord Coke :

1. What was the law before the Act was passed,-
2. What was the mischief or defect for which the law had not provided; 3. What remedy Parliament has appointed; and 4.
The reason of the remedy."

15. We may also in this connection refer to the fact that in the Order for the assessment of 1950-51 which was the first assessment on the company under the Indian Income-tax Act after that Act was extended to Travencore-Cochin, the loss of 1123 was ascertained and there was an express direction to carry forward that loss also to the next year. There was no profit or income in 1950-51 against which the losses of 1123, 1124, 1125 and 1950-51 could be set off, and the direction in the assessment order was that the entire loss for those four years amounting to Rs. 14,003-1-3 "will be carried forward". That order has been set out in paragraph 3 above of this judgment. The direction to carry forward the loss could have been made only because of the view then taken by the Income-tax Officer that the loss of 1123 could be carried forward for more than the period of two-years allowed by Section 32(2) of the Travencore Income-tax Act, for if the loss could not have been carried forward for more than two years no useful purpose could have been served by giving the direction: "This will be carried forward." If the direction was considered to be wrong it would not also have been allowed to stand, for the Commissioner of Income-tax could have vacated that direction revision proceedings taken suo motu. It may be that if, under the law, the company could not carry forward the loss of 1123 for more than two years this direction in the assessment order of 1950-51 would not be binding in the subsequent proceedings and the company might be assessed for 1951-52 ignoring the same. Wrong understanding of the law by the Income-tax Officer will not, of course, confer a right on the assessee if the law is otherwise or bar the income-tax authorities to proceed according to the correct law subsequently. All that we desire to point out here is only how the Income-tax authorities themselves understood the law to be before the assessment of 1951-52 was made on the company.

16. Reading Section 3 of the Taxation Laws (Part B States) (Removal of Difficulties) Order, 1950, in the light of all the circumstances mentioned in paragraph 13 above and the principles referred to in paragraph 14 and also having regard to the fact that the Taxation Laws (Part B States) (Removal of Difficulties) Order, 1950, was expressly passed in exercise of the powers conferred on the Central Government by Section 12 of the Finance Act, 1950, which itself was enacted for the purpose of providing a machinery for removing difficulty in giving effect to the provisions of the extended Act, the right and proper construction of Section 3 of that Order appears to us to be the construction contended for by the company's counsel and not the construction the department's counsel seeks to put upon it. There is no case that any 'capital loss' in respect of which the company would be entitled to the larger relief under Section 32(2) of the Travencore Income-tax Act is included in the loss of 1123 which, as has been stated already, the company seeks to carry forward and set off against the income of 1951-52 and which has also been ascertained and fixed in the assessment order of 1950-51. Therefore, for the reasons stated in paragraphs 8 to 14 above we hold that the company is entitled to carry forward the loss of 1123, mentioned in the assessment order of 1950-51 and disallowed in the order of 1951-52, for a period of six years as provided in Section 24(2) of the Indian Income-tax Act and not merely for the period of two years mentioned in Section 32(2) of the Travencore Income-tax Act.

17. Question No. 2 relates to the company's contention that the damages which it has received

from the lessees for breach of Clauses 14 and 16 of the lease deed is not an item of income, profit or gain and is only a capital or casual receipt and is not therefore assessable to tax. Clause 14 provided that during the continuance of the lease and for a further period of three years after its expiration the lessees should not either directly or indirectly work for any other rubber goods manufacturing concern or themselves carry on any such concern except continuing their business at Kanjirapally and that in the event of the breach of this provision they were to pay to the company a lump sum of Rs. 10,000 as compensation and Clause 16 provided that if the lessees discontinued the lease before the termination of the period fixed in the lease deed they were to pay to the lessors a sum of Rs. 10,000 by way of liquidated damages for the discontinuance. As has been stated already, out of the amount received by it from the lessees under the compromise in 1950, the company credited a sum of Rs. 7075-1-6 towards damages under Clause 14 and a sum of Rs. 8050-1-6 towards damages under Clause 16 and it was thus that the sum of Rs. 15,125-3-0 mentioned in question No. 2 was made up of. According to the company, both these amounts (i.e., both Rs. 7075-1-6 and Rs. 8050-1-6) are capital receipts not assessable to tax; and according to the department, both of them are revenue receipts assessable to tax.

18. The vexed question as to what would be capital receipt and what revenue receipt has come up for consideration before the Supreme Court in *Commissioner of Income-tax and Excess Profits Tax, Madras v. South India Pictures Limited*[5], On the question whether the disputed receipt in that case was a capital receipt or a revenue receipt

[5](1956) 29 ITR 910 : (AIR 1956 SC 492)

there was a difference of opinion, their Lordships S.R. Das, C.J. and Venkatarama Ayyar, J., holding that it was not a capital receipt but a revenue receipt and Bhagavathi, J., holding otherwise Das, C.J., who delivered the judgment of the majority Judges says at page 915 (of ITR) of the report :

> "It is not always easy to decide whether a particular payment received by a person is his income or whether it is to be regarded as his capital receipt. Income said Lord Wright in *Kamakshya Narain Singh v. Commissioner of Income-tax, B and O*[6] is a word of the broadest connotation and difficult and perhaps impossible to define in any precise general formula. Lord Macmillan said in *Van Den Berghs Ltd. v. Clark*[7], that though in general the distinction between an income and a capital receipt was well recognized and easily applied, cases did arise where the item lay on the border line and the problem had to be solved on the particular facts of each case.

No infallible criterion or test can be or has been laid down and the decided cases are only helpful in that they indicate the kind of consideration which may relevantly be borne in mind in approaching the problem. The character of the payment received may vary according to the circumstances. Thus the amount received as consideration for the sale of a plot of land may ordinarily be a capital receipt but if the business of the recipient is to buy and sell lands, if may well be his income. The problem that confronts us has to be approached keeping in mind the different kinds of consideration taken into account in the different cases. The assessee before us is a company carrying on a business and it received the sum in question in connection with that business. We have, therefore, to ask ourselves as to what is the substance of the matter from the point of view of a businessman;

.....

The business of the assessee in that case was to distribute films, and for this purpose it had entered into agreements with various concerns. The agreements entered into with one concern were terminated before the expiry of the period stipulated for and the disputed amount was received by the assessee as compensation for the termination of those agreements. The reason for holding that amount to be a revenue receipt, and not a capital receipt, is stated by His Lordship at pages 915 to 917 (of ITR) : (at PP. 495-496 of AIR) of the report as follows :

> "For the purpose of this distribution business the assessee obviously had arrangements with the proprietors of different cinema halls. If any producer failed to deliver any film as agreed then the exigencies of the assessee's business would certainly have required the assessee to treat that agreement as terminated by breach and to enter into, another agreement for securing the distribution right in some other film so as to enable it to fulfil its engagement with the proprietors of the cinema halls by distributing the new film in the place of the one that had not been supplied.

Likewise if a particular film secured by the assessee failed to attract public enthusiasm, business exigencies might well have required the assessee to enter into an

[6](1943) 11 ITR 513: (AIR 1943 PC 153)
[7](1935) 8 ITR (Suppl) 17

agreement with the producers, concerned to cancel the agreement for distribution of that film and to enter another agreement with the same or other producers for acquiring the distribution right in another film likely to bring a better box-office collection. The termination of the agreement in each of the circumstances hereinbefore mentioned could well be said to have been brought about in the ordinary course of business and money paid or received by the assessee as a result of or in connection with such termination of agreements would certainly be regarded as having been so paid or received in the Ordinary course of its business and therefore a trading disbursement or trading receipt. There was no covenant made by the assessee with Jupiter Pictures not to enter into agreement with other producers or not to distribute films secured from other producers. In fact in the accounting year the assessee had distribution rights in respect of eleven films including these three. These three agreements would have come to an end on the expiration of the period of five years from the respective dates of release of the films and had only a part of the period to run, a fact which may also be relevantly borne in mind. The cancellation of these agreements must have left the assessee free, if it so chose, to secure other films which could be distributed in the place of these films and which might have brought in better box-office collections. In the language of Lord Hanworth, *M.R., in Short Bros. Ltd. v. Commissioners of Inland Revenue*[8], the sum paid to the assessee was not truly compensation for not carrying on its business to adjust the relation between the assessee and the producers of the films. The agreements which were cancelled were by no means agreements on which the whole trade of the assessee had for all practical purposes been built and the payment received by the assessee was not for the loss of such a fundamental asset as was the ship managership of the assessee in *Barr, Crombie and Co. Ltd. v. Commissioners of Inland Revenue*[9], Nor can one say that the cancelled agreements constituted the frame-work or whole structure of the assessee's profit making apparatus in the sense the agreement between the two margarine dealers concerned in 1935-3 ITR Suppl 17, was. Here were three agreements entered into by the assessee in the ordinary course of his business along with several similar agreements. These three agreements

were by mutual consent put an end to. The termination of these three agreements did not radically or at all affect or alter the structure of the assessee's business. Indeed the assessee's business of distribution of films proceeded apace notwithstanding the cancellation of these three agreements."

19. The principles to be deduced from the above judgment for determination of the question whether a particular receipt is a capital receipt or revenue receipt are :

(i) the substance of the transaction from the point of view of a businessman has to be ascertained;

(ii) if the agreement cancelled related only to some of the transactions carried on in the ordinary course of the business of the assessee, the compensation paid is money received by the assessee during the ordinary course of his business and therefore trading or revenue receipt;

(iii) if the cancelled agreement was one on which the whole trade of the assessee had for all practical purposes been built, the cancellation of the

[8]1927-12 Tax Cas 955, 973

[9]1945-26 Tax Cas 406

agreement would result in the termination of the assessee's business itself (as distinguished from the termination of transactions entered into during the ordinary course of its business) and so the compensation paid is a capital receipt and not a revenue receipt; and

(iv) even if the agreement was not one on which the whole business or trade of the assessee had been built if its cancellation radically affected or altered the framework or whole structure of the assessee's business, the compensation paid is capital receipt and not revenue receipt.

20. From the assessment orders on the company and the lease agreement (Annexure-A) it is clear that, except, the factory in question, the company had no other factory and that after the lease was granted till at least its termination the company was not doing any other business at all. The company had not also granted any other lease either before this lease was granted or during the period it was in force. The lease transaction with the lessees was practically the only source of its income after the lease was granted till the termination thereof. In other words, after the factory was leased to the lessees the business of the company consisted only of this lease which it had given to the lessees and nothing else. Since the company had stopped its normal activities when it granted the lease and was doing no other business thereafter, the termination of the lease by the lessees before the expiry of the period fixed in the lease deed would necessitate fresh outlays of capital expenditure for restarting the working of the factory by it at a time when, under normal circumstances, it would not have been ready or prepared to incur such expenditure. This was the reason for the provision in Clause 16 of the lease deed that if the lessees discontinued the lease before the efflux of the period they should pay Rs. 10,000 by way of liquidated damages. In the light of the principles laid down by the Supreme Court in the passage extracted above from the (1956) 29 ITR 910 : AIR 1956 SC 492, there can be no doubt that from the point of view of the company the damages stipulated for in Cl., 16 are of the nature of capital receipt and not revenue receipt. The lease was granted in 1941 and the period fixed was 15 years. It was terminated in

1950, and the termination radically affected and altered the framework and whole structure of the company's business inasmuch as it put an end to the lease from which the company was deriving its income till then and necessitated the company to restart the working of the factory itself, incurring fresh outlays of capital expenditure. Until the termination of the lease the company had to do nothing and got its income from the rent paid by the lessees.

21. In another case which is very similar to the present case, *Hari Kailash and Co. v. Income-tax Commissioner*[10], Malik, C.J., has pointed out what compensation or damages paid under contracts would be capital receipts and what revenue receipts. The assessee firm in that case had entered into a contract to finance a business of another company for five years. The agreement regulated the conditions under which the assessee firm was to carry on the trade or business and the assessee firm also acquired certain rights under it. For cancellation of the agreement before the agreed period of five years, the assessee firm received a sum of Rs. 37,248 as compensation from the company it was to finance, and the question for decision in that case was whether this amount was a capital receipt or a revenue receipt. In the present case,

[10] AIR 1953 All 170

under the provisions of the lease agreement, the assessee i.e., the company had to make available to the lessees the factory and its machines and also the services of certain experts for a period of 15 years and had the right to receive in consideration thereof the rent stipulated for in the lease agreement. The amount of Rs. 8050-1-6 received by the company is the compensation for the termination of this agreement before the expiry of the period. Thus, the facts of the two cases are very similar.

The only difference between the two cases is that the compensation for the termination was fixed in the Allahabad case by a second agreement entered into at the time of the termination, whereas provision had been made in the case before us in the original agreement itself for payment of compensation in the case of termination of the agreement before the period fixed in it. At page 173 of the AIR, Malik C.J., says :

> "..... Lord Moncrieff divided two classes of cases of compensation paid for termination of contracts as follows :
> "(1) a contract may be made by a trader which is merely directed to result in trading profits being made;
> (2) a contract may be made by a trader which is directed to regulate the conditions under which he is to carry on his trade'.

In the first class of cases, if the contract is terminated or a breach thereof is made and compensation or damages are received it might be treated as trading profits. In the second class of cases, compensation received for the termination of a business cannot be treated as trading profit as it was paid for the termination of the trade or business. The amount received in such a case would ordinarily fall within the rule laid down in *Commissioner of Income Tax, Bengal v. Shaw Wallace and Co*[11], and would not be taxable, In one case, one gives up the source from which the income arises; in the other one merely gives up anticipated profits which would have accrued to him if the contract had not been discontinued or terminated, for cash payment. In the case before us, there was a contract entered into by the assessee firm on 9-4-1940, which was then run for a period of five years. It was to regulate the conditions under which the assessee firm was to carry on the trade or business. It acquired, under this agreement, certain rights and was not

put under certain liabilities. By the cancellation agreement of 22-11-1941, all these congeries of rights that it had acquired under the first agreement were terminated for a certain consideration. The compensation paid for termination of those rights is not taxable income and income-tax cannot be charged on that sum. The amount of Rs. 37,248 cannot, therefore be said to be a revenue receipt. This is our answer to the question formulated by the Tribunal". Thus, damages paid under contracts are divided by the learned Chief Justice into two classes, one received for the non-performance of a contract, entered into in the course of business for the purpose of making trading profits, and the other, damages paid for the discontinuance of the business itself. This division is practically the result of the application of the principles stated in paragraph 19 above. As the damages provided for in clause 16 are in respect of the discontinuance of the business from which the company was deriving its income till the termination of the lease the amount credited thereunder, namely, Rs. 8050-1-6, hap to be held to be a capital receipt and not revenue receipt.

[11]6 ITC 178 : (AIR 1932 PC 138)

22. Reliance has been placed by the department on the decision of the Calcutta High Court in *Cossimbazar Raj Wards Estate v. Commissioner of Income-tax*[12], in support of the contention that when a lease is terminated before the expiry of the period provided for in the lease deed and the lessee pays money to the lessor in consequence of such termination the amount received by the lessor is a revenue receipt and not a capital receipt. The lease in that case was a mining lease of some colliery lands and was granted for a period of twenty years. It was specifically provided in the lease deed that the lessees were at liberty to abandon the lease before the period of the lease expired if they paid up in full the rents and royalties of every description and that if any coal remained unworked for any reason whatsoever royalty would be payable in the same manner as if the coal had been worked, as soon as the coal should have been abandoned. When the lease was terminated by the lessees before the expiry of the period, there was unworked coal in the coal mines, and the amount paid by the lessees to the lessors represented the amount which they were to pay in respect of this coal under the agreement mentioned above. The High Court held that on a consideration of the substance of the transaction it was clear that the Estate received the payment not as consideration for the termination of the lease agreement but as royalty on the abandoned coal pursuant to the terms of the agreement and as such it was a revenue receipt and not a capital receipt. The facts of the present case are entirely different. The sum of Rs. 8050-1-6 received under Clause 16 could have been received, and was actually received, only as consideration for the termination of the lease which was the main fame-work or structure of the company's business and the only source of its income. The present case, so far as the payment under Clause 16 is concerned, is governed by the principles laid down in 1956-29 ITR 910 : AIR 1956 SC 492 and AIR 1953 Allahabad 170 and (1945) 14 ITR 377 : AIR 1947 Calcutta 87, can have no application to it.

23. The purpose of the conditions in Clause 14 of the lease deed is only to ensure the company's profits after the termination of the lease. The lessees had agreed by the provisions in Clause 14 not to compete with the lessors in certain fields for sometime after the termination of the lease or the expiry of the period, and also not to carry on similar enterprises during the period of the lease itself, and it was for the non-performance of those conditions that damages were provided for in Clause 14. The damages paid under Clause 14 would, therefore, fall in the first of the classes of damages mentioned in paragraph 21 above, namely, damages for the non-performance of a contract entered into in the course of business for the purpose of making trading profits. That

being so, the damages received under Clause 14 of the lease deed will have to be treated as revenue receipt and not capital receipt.

24. It was also contended by the company's counsel that, at any rate, this amount of Rs. 7075-1-6 should be treated as a casual receipt and held to be not assessable on that basis. In the first place it is impossible to hold that the payment in question was a casual receipt since the liability for payment was clearly anticipated and definitely provided for in the lease deed itself - (see the observations of Ormond, J., in (1945) 14 ITR 377 at p. 395 : (AIR 1947 Calcutta 87 at p. 93) :

> "This payment was expressly provided for in the lease and therefore it was
> foreseen, known, anticipated and provided for as it was put by Dr. Gupta. It has its source in the agreement itself where it is clothed with the nature of royalty. In these circumstances it cannot be held to be a casual receipt").

[12](1945) 14 ITR 377 : (AIR 1947 Cal 87)

In the second place, it is not every casual receipt that is exempt from liability to assessment. Under Section 4(3)(vii) of the Income-tax Act it is only receipts of a casual and non-recurring nature which do not arise from business or the exercise of a profession, vocation or occupation that are exempt from assessment. As has been pointed out in *Bishweshwar Singh v. Commissioner of Income-tax, B. and O*[13]. a receipt resulting from the carrying on of a business cannot be regarded as casual for purposes of income-tax assessment. The agreement under Clause 14 in the present case was an agreement made in the ordinary course of business to safeguard against competition and, therefore, the payment of compensation thereunder cannot be said to be one not arising from business. We, therefore, hold that the amount of Rs. 7075-1-6 is clearly liable to assessment.

25. Towards the close of paragraph 3 of the order of the Appellate Tribunal, disposing of the appeal, it has said :

> "It is stated that the matter was ultimately referred to arbitrators who awarded Rs. 23,000 odd which is received by the assessees in full and final settlement of all claims. Out of this, in the books of the assessees, after adjusting rents etc., due, Rs. 7075-1-6 and Rs. 8050-1-6 totalling Rs. 15,125-3-0 have been shown as compensation received in respect of damages sustained under Clauses 14 and 16 respectively. The assessee however has not filed a copy of the award and it is said that the award was oral."

In paragraph 4 of its order the Tribunal has said further;

> "It is admitted by the assessee that the residue of Rs. 15,125-3-0 out of the aforesaid award of Rs. 23,000 odd received, has been allocated as Rs. 7,075-1-6 and Rs. 8,050-1-6 between compensation for breach of Clauses 14 and 16 respectively arbitrarily and without any basis. Besides the assessee has not shown that it could have suffered any damage at all under Clause 14, as the contract was terminated within the stipulated period of 15 years, when there can be no question of any competition to the detriment of the

assessee's interest; ....."

in paragraph 6 of the statement of the case also the Tribunal has said :

"There is no evidence of either the arbitration itself or the details of the award if any." Thus, the Tribunal seems to doubt whether there was any arbitration and whether under the arbitration damages had been awarded under Clauses 14 and 16. But the Income-tax Department had no case at all before either the Income-tax Officer, or the Appellate Assistant Commissioner, or even the Appellate Tribunal, that there was no arbitration and that damages had not been awarded under Clauses 14 and 16 of the lease agreement. In the Income-

[13]1955-27 ITR 376 : (AIR 1955 Pat 96)

tax Officer's order it is specifically stated :

"After sometime the suits were compromised by the mediation of Sri Venkatachalam Ayyar of Kottayam. It was agreed upon that towards the entire satisfaction of all the amounts then found due to the assessee as per the records and also towards the claims made in the suits under the terms of the lease deed the lessees were to pay to the assessees a round sum of Rs. 20,000. The parties agreed to this and assessee company thus got Rs. 20,000. Along with this the assessees got from the lessees Rs. 3,311 also on account of certain other payments already made by them on behalf of the lessees ..... The balance of Rs. 15,125 was treated by the company as compensation received under Clauses 14 and 16."

26. The plaints in the suits brought by the company on lease deed are among the records of the case and show that the claims in those suits included the claims for damages as per the provisions of the lease deed. The Appellate Assistant Commissioner's order also shows that there was no dispute before him either about these matters. The appeal before the Appellate Tribunal was filed by the company and not by the department; and there is nothing to show that the department had ever questioned the factum of the arbitration or the details of the award as set up by the company. The Tribunal was not, therefore, justified in doubting the factum of the arbitration and the details thereof; As the total damages paid by the lessees was Rs. 15,125-3-0 and the maximum damages which could be claimed under each of the Clauses 14 and 16 was only Rs. 10,000 it is obvious that the award must have been made under both clauses. Since the award was the result of an arbitration the probabilities are that the maximum amount of damages under each clause would not have been awarded and the correctness of the appropriation of the amount towards the two clauses i.e., Rs. 7075-1-6 towards Clause 14 and Rs. 8050-1-6 towards clause 16 was not, as has already been stated, disputed by the department at any time. Although in view of the conclusions we have reached in paragraphs 23 and 24 above regarding the amount of Rs. 7075-1-6 credited in the company's accounts as damages received under Clause 14, it is not necessary to consider the correctness of the Tribunal's observation to the effect that the company could not have suffered any damages at all under Clause 14 and that there was therefore no-scope for award of damages by the arbitrator under the said clause; it may be pointed out that in this matter also the Tribunal was laboring under a misapprehension. The Tribunal's view that there was no scope for the award of damages under Clause 14 is wrong. One of the conditions under Clause 14 was that

the lessees were not to engage themselves in a competitive business for three years after the termination of the lease. It was to discharge them from this obligation that damages under Clause 14 were awarded and paid. The correctness of the appropriation under each head was also not disputed by the department at any time.

27. In the result, our answers to the questions referred are :

> Question No. 1 : Under the provisions of the Indian Income-tax Act the petitioner (i.e. the company) is entitled to carry forward the loss for a period of six years notwithstanding the fact that during the period when the loss had occurred the law applicable was the Travencore Income-tax Act.
>
> Question No. 2 : Out of the amount of Rs. 15,125-3-0 received by the petitioner (i.e., the company) from the lessees of the factory towards damages, a sum of Rs. 8050-1-6 is not assessable to income-tax and the balance amount of Rs. 7075-1-6 is assessable.

28. The questions are answered accordingly, and the department is directed to pay two thirds of the costs of the petitioner (company). The advocate's fee for the reference is fixed at Rs. 150 and as per the above direction regarding costs the petitioner (company) will be entitled to get Rs. 100/- as advocate's fee from the department.

Answer accordingly.