

PATNA HIGH COURT

Traders and Miners Ltd

Vs

Commissioner of Income Tax

Misc. Judicial Case No. 4 of 1953

(Ramaswami and Choudhary, JJ.)

19.10.1954

ORDER

Choudhary, JJ.

1. In this case the assessee company had purchased, on 16-5-1934, six pies share in the Zamindari of Masnodih Gaddi from one Tufani Singh for a sum of Rs.40,000. On 3-3-1933, the assessee company similarly purchased 3 annas 9 pies share of the same Zamindari for Rs.1,27,500 from Christian, Mica Company.

2. There are 120 Mica mines located in the portion of the zamindari acquired by the assessee company. On 7-12-1946, the assessee company executed an indenture of lease in favour of Kedarnath Singh for a consideration of Rs.92,000 and a reserve rent of Rs.3,000 per year. The lease was granted for 99 years and comprised an area of 325 acres of the Zamindari. The lease related to surface right together with nine mica mines located in the area demised. The Income-tax Officer determined that the cost of the mineral right with respect to the nine mines transferred to the company would be Rs.12,562, on a proportionate basis.

3. After deducting this amount from the Salami of Rs.92,000 which the Company received from Kedarnath Singh the Income-tax Officer found that the assessee company had made a capital gain of Rs.79,438 and taxed this amount under Section 12B, Income-tax Act. The assessee preferred an appeal to the Appellate Assistant Commissioner but the appeal was dismissed.

4. A further appeal was taken to the appellate Tribunal who took the view that the cost price of the nine mines would be Rs.20,000 and the assessee was liable to be taxed only on the amount of Rs.72,000. It was argued before the Tribunal on behalf of the assessee that the transaction was not hit by Section 12B of the Act, but this argument was rejected by the Tribunal. It was contended on behalf of the assessee that Section 12B of the Act was constitutionally invalid, but this contention also was rejected by the Tribunal. At the instance of the assessee the Tribunal has submitted the following questions of law for the opinion of the High Court:

"(1) Whether the indenture dated 7-12-46 was a sale or transfer of a capital asset within

the meaning of Section 12B(1), Income-tax Act? and (2) whether Section 12B, Income-tax Act imposing income-tax on capital gains was ultra vires?"

The first question argued in this case is whether the transaction of lease dated 7-12-1946, was a transfer of a capital asset within the meaning of Section 12B, Income-tax Act. The argument put forward by Mr. Dutta on behalf of the assessee is that a transaction in the nature of a lease would not amount to a transfer of a capital asset and the amount of the Salami received by the assessee company was not taxable under the provisions of Section 12B of the Act.

5. The question at issue depends on the proper interpretation of Section 12B(1), which is in the following terms:

"The tax shall be payable by an assessee under the head 'Capital gains' in respect of any profits or gains arising from the sale, exchange or transfer of a capital asset effected after the 31st day of March, 1946, and before the 1st day of April, 1948; and such profits and gains shall be deemed to be income of the previous year in which the sale, exchange or transfer, took place....."

The expression "capital asset" is defined in Section 2(4A) of the Act as:

"property of any kind held by the assessee whether or not connected with his business, profession or vocation but does not include (I) any stock-in-trade, consumable stores or raw materials held for the purposes of his business, profession or vocation; (II) personal effects, that is to say, moveable property; and (III) any land from which the income derived is agricultural income."

6. It should be noticed in this context that Section 6 of the Act has also been amended by including therein an additional head of income and that additional head is "Capital gains". The contention advanced on behalf of the assessee is that a "transfer of a capital asset" referred to in Section 12B should be interpreted to mean a permanent and out and out transfer of title and a lease of mineral asset even for a period of 99 years would not come within the ambit of Section 12B.

7. In our opinion there is no warrant for interpreting the expression "transfer of a capital asset" in Section 12B in this narrow and restricted sense.

8. We think that the expression "transfer" in the section includes not only a permanent transfer but also a temporary transfer of title to the property in question and a lease of mines for any period would fall within the ambit of Section 12B, of the Act. It was also contended by Mr. Dutta that a transaction of a lease was not tantamount to a transfer of title but that a mere contractual right was created. We do not think that this argument is correct. A lease of land is a transfer of interest in the land and creates a right 'in rem', and there is a transfer of title in favour of the lessee though the lessor has right of reversion after the period of the lease terminates. For these reasons we are satisfied that the transaction of the lease granted by the assessee company on 7-12-1946 in favor of Kedarnath Singh was a transfer of a capital asset within the meaning of

Section 12B of the Act and the gains arising to the assessee company on account of this transfer of the capital asset was rightly taxed by the Income-tax authorities.

9. In support of his argument counsel for the assessee referred to - '*Hind Estates Ltd. v. C.S. Peters*', (A). But the ratio of that case has no bearing on the question we have to determine in the present case. The question for decision in that case was whether the word 'transfers' in Section 4 of the Payment of Taxes Act, 1949, should be interpreted so as to include lease of certain properties for 99 years from certain persons. It was held by the Calcutta High Court that Section 4 of the Payment of Taxes Act of 1949, must be given a restricted interpretation in the context of Section 3 of Ordinance 3 of 1948, where the same expression has been used but in a restricted sense. Section 3 of the Ordinance expressly referred to transactions which required to be registered under Section 17(a)(b),(c), and (e) of the Registration Act. Section 17(d) which deals with lease of immovable property from year to year or for any term exceeding one year was expressly omitted from Section 3 of the Ordinance. For this reason it was held by Das Gupta, J. that Section 4 of the Payment of Taxes Act of 1949, did not apply to lease of immovable property. It is manifest that the 'ratio' of this case has no application to the present case and the first question referred to the High Court must be answered in favour of the Income-tax Department and against the assessee. The second question relates to the constitutional validity of Section 12B of the Act. The argument of Mr. Dutt is that the Central Legislature was not competent to enact such a legislation by virtue of any authority conferred by item 55 of List 1, 7th Schedule of the Government of India Act. Item 55 reads as follows "Taxes on the capital value of the assets, exclusive of agricultural land, of individuals and companies, taxes on the capital of companies". The argument advanced on behalf of the assessee is that Section 12B does not fall within the ambit of item 55 and the Central Legislature was not competent to enact the legislation. Mr. Dutt, however, conceded that if Section 12B was confined in its operation to profits arising from sale or exchange of a capital asset, the legislation would be intra vires. But the point taken by the counsel is that profits or gains arising out of a transfer of a capital asset in the nature of lease would not be covered by item 55 of List 1 of the 7th Schedule and Section 12B of the Act would be ultra vires so far as it purported to impose a tax on profits or gains arising from the transfer of a capital asset in the nature of a lease.

We are unable to accept this argument as sound. In our opinion the Central Legislature has validly enacted Section 12B, Income-tax Act, in exercise of the authority conferred upon it by item 55 of List 1 of the 7th Schedule. The question at issue is the question of proper classification or characterization of the law. We are satisfied that the legislation enacted in Section 12B is in pith and substance legislation relating to tax on the capital value of the assets. What is the standard by which the "pith and substance" of a law may be determined?

10. The answer is furnished by Latham C.J. in the 'Uniform Tax Case, 65 Comm-W LR 424 (B)'

"The true nature of a law is to be ascertained by examining its terms and, speaking generally ascertaining what it does in relation to duties, rights or powers which it creates, abolishes or regulates. The question may be put in these terms 'what does the law do in the way of charging or creating or destroying duties or rights or powers?' "

It is true that Section 12B, Income-tax Act has imposed certain conditions before tax can be

assessed. The first condition is that there must be a transfer, sale or exchange of the capital asset and the legislature states that the assessee shall pay the tax of the gains or profits arising out of this transaction. In the second place, Section 12B enunciates in what manner the capital value of the assets should be calculated for the purpose of imposing tax. The provisos to Section 12B indicate that the Department must give deduction for the actual cost of the asset to the assessee and also the expenditure on the transaction incurred by the assessee. In other words, the Legislature did not intend to tax the full value of the capital asset as represented by the sale proceeds or the consideration for the transfer or exchange, but the Central Legislature permitted the assessee to deduct from the sale proceeds or consideration the actual cost of the capital asset and also the expenditure incurred by the assessee upon the transaction. If the transaction was a lease and not an outright sale, the amount of consideration would be less and the Income-tax Department would impose tax on the smaller amount realised by the transfer of the capital asset. But that does not mean that the tax is not a tax on value of the capital asset. The quantity (sic.) of the tax is the same though there may be quantitative difference. If the transaction is by way of lease, only the computation of profit would be affected. The difference is only a difference in computation. The quality of the tax is not affected, and, in our opinion, the tax contemplated by Section 12B of the Act falls within the ambit of item 55 of List 1 of the 7th Schedule. It follows that Section 12B is constitutionally a valid piece of legislation and the second question referred to the High Court must also be answered in favour of the Income-tax Department and against the assessee. Reference was made in the course of argument to the decision of the Bombay High Court in - '*J.N. Duggan v. Commissioner of Income Tax, Bombay City*²',

11. It was held in that case by both the learned Judges that the Income-tax (Amendment) Act (22 of 1947) by which Section 12B was for the first time introduced was a valid piece of legislation and it was not ultra vires for the Indian Legislature. Chagla, C.J. proceeded upon the view that Section 12B fell within the ambit and scope of item 55 of List 1 of the 7th Schedule. But Tendolkar, J. was of the opinion, that Section 12B was legislation with respect to income and was covered by item 54 of List 1 of the 7th Schedule. With great respect we think that the view taken by Chagla, C.J. is correct and we have already expressed our reasons for taking same view in this case.

12. For the reasons expressed we hold that both the questions referred to the High Court must be answered in favour of the Income-tax Department and against the assessee.

13. The assessee must pay the costs of the reference. Hearing fee Rs.250.

Answers accordingly.

Cases Referred.

¹1951-20 ITR 67 (Cal)

² AIR 1952 Bom 261