PRIVY COUNCIL.

COMMISSIONER OF INCOME-TAX, BENGAL

v.

SHAW, WALLACE AND COMPANY.

P. C.*
1932

Feb. 5, 9, 11;
March 14.

[On Appeal from the High Court at Calcutta.]

Income-tax—"Income"—Income from business—Compensation for cessation of agency—Indian Income-tax Act (XI of 1922).

The term "income" in the Indian Income-tax Act, 1922, connotes a periodical monetary return "coming in" with some sort of regularity, or expected regularity, from definite sources; the source is not necessarily one which is expected to be continuously productive, but it must be one whose object is the production of a definite return, excluding anything in the nature of a windfall. The expansion into "income, profits and gains" is more a matter of words than of substance. The fundamental idea of "business" as a source of taxable income under section 6 (*iv*) is the continuous exercise of an activity; there must be a business "carried on" by the assessee.

The respondents carried on business in India as merchants and agents of various companies. For several years before 1928 they acted as distributing agents in India for two oil companies, but without any formal agreements. The two oil companies combined and decided to make other distributing arrangements; each terminated the respondent's agency, and in 1927-28 paid them compensation for its cessation.

Held that the sum so received by the respondents was not taxable income under section 6 (*iv*) (business) because it was not the produce, nor the result, of carrying on the agencies of the oil companies in the year in which they were received; nor under section 6 (*vi*) (other sources) for the same reason.

The Indian Income-tax Act differs materially from the English income-tax statutes, and, at any rate in the present case, decisions under the English statutes are of little assistance in applying the Indian Act.

In re *Turner Morrison & Co., Ltd.* (1) doubted.

Judgment of the High Court (2) affirmed.

Appeal (No. 108 of 1931) from a judgment of the High Court (January 13, 1931) upon a reference by the Commissioner of Income-tax under section 66, sub-section (2) of the Indian Income-tax Act, 1922.

The matter for consideration in the appeal was, in substance, whether the respondents, who carried on business as merchants and agents in Calcutta and elsewhere in India, were chargeable to income-tax

**Present*: Lord Blanesburgh, Lord Tomlin and Sir George Lowndes.

(1) (1928) I. L. R. 56 Calc. 211. (2) (1931) I. L. R. 58 Calc. 1153.

1932

Commissioner of Income-tax, Bengal
v.
Shaw, Wallace and Company.

under the above Act in respect of compensation paid to them for the termination of agencies for two oil producing companies.

The facts of the case and the three questions referred appear from the judgment of the Judicial Committee.

The High Court, by a judgment delivered by Rankin C. J. and concurred in by C. C. Ghose and Buckland JJ., answered the first question in the affirmative, thereby holding that the sum of Rs. 9,83,361 (being the compensation received less admitted deductions) was a capital receipt and, therefore, did not come within the computation of the profits of the respondents' business. Having regard to that conclusion, no answer was returned to the second and third questions. The Court was, however, of opinion, upon the authority of *In re Turner Morrison & Co., Ltd.* (1), that the receipt arose out of the business; also that the exemption in section 4, sub-section (*3*) (*vii*) of the Act did not apply to the case.

Dunne K. C. (with him *R. P. Hills*) for the appellant. The compensation (less the admitted deductions) is chargeable to tax under section 6 (*iv*) of the Indian Income-tax Act, 1922, under the head "business." The agencies in respect of which the compensation was paid were part only of the respondents' business, and their business as merchants and agents continued after the payment; the compensation was a profit of the business in the year of account. There was no transfer of goodwill or any other dealing with the capital. As both the Commissioner and the High Court found that the compensation arose out of the business, it was chargeable to tax unless the assessees showed that it came within the exemptions in section 10, or that it was capital receipt not chargeable to tax. The Indian Act does not make the clear distinction between capital and interest, which there is under

(1) (1928) I. L. R. 56 Calc. 211.

the English statutes; that is shown by section 4, sub-section (*3*) (*v*). The judgment of the High Court is not consistent with its judgment *In re Turner Morrison & Co., Ltd.* (1). It was based upon *Glenboig Union Fireclay Co., Ltd.* v. *Commissioners of Inland Revenue* (2) and *Chibbett* v. *Joseph Robinson and Sons* (3), both of which are distinguishable. The former case was decided upon the ground that there had been a sterilization of a capital asset. In the latter case, the assessees had rights under the articles of association and received a capital sum to release them. The decision was merely that there was evidence to support the finding of the Commissioner, whereas in the present case the Commissioner held that the receipt was not of a capital nature; the observations of Rowlatt J., relied on, were *obiter*. That the compensation received in this case was chargeable to tax is supported by *Hancock* v. *General Reversionary and Investment Co.* (4), *Commissioners of Inland Revenue* v. *Newcastle Breweries, Ltd.* (5), *Short Bros., Ltd.* v. *Commissioners of Inland Revenue* (6), *Gloucester Railway Carriage and Wagon Co., Ltd.* v. *Commissioners of Inland Revenue* (7), *Ensign Shipping Co., Ltd.*, v. *Commissioners of Inland Revenue* (8), *Burmah Shipping Co.* v. *Commissioners* (9), *J. Gliksten & Son* v. *Green* (10). In *Anglo-Persian Oil Co.* v. *Dale* (11) it was held that compensation paid by the then appellant company in the same circumstances as in this case was a revenue payment and therefore deductible in arriving at their net profits.

Latter K. C. (with him *Cyril King*) for the respondents. The observations of Rowlatt J. in

(1) (1928) I. L. R. 56 Calc. 211.
(2) (1922) 12 Tax Cas. 427.
(3) (1924) 9 Tax. Cas. 48.
(4) [1919] 1 K.B. 25.
(5) (1927) 12 Tax Cas. 927; 43 T. L. R 476.
(6) (1927) 12 Tax Cas. 955; 136 L. T. 689.
(7) (1925) 12 Tax. Cas. 720; [1925] A. C. 469.
(8) (1928) 12 Tax. Cas. 1169; 138 L. T. 180.
(9) (1930) 16 Tax Cas. 67.
(10) [1929] A. C. 381.
(11) [1932] 1 K.B. 124.

1932

Commissioner of Income-tax, Bengal
v.
Shaw, Wallace and Company.

Chibbett's case (1) referred to in the judgment of the Chief Justice were correct and are directly in point. The business there continued after the payment, as it did in this case. The money received was compensation for loss of part of the business as distinct from earnings of the business. Income is something which flows from the property or trade as distinct from something received in place of the property or trade, in whole or in part: *Commissioners of Inland Revenue* v. *Blott* (2) and *Pool* v. *Guardian Investment Trust Co.* (3), referring to *Eisner* v. *Macomber* (4). The idea of income flowing from a source is embodied in the Indian Act in sections 4 and 12. The series of English cases referred to for the appellant are distinguishable upon their facts. The decision in the *Anglo-Persian Oil Co.* case (5) cannot be applied; the effect of an exemption or proviso cannot be used to extend the scope of a statutory provision: *Commissioners for Special Purposes of Income Tax* v. *Pemsel* (6), *West Derby Union* v. *Metropolitan Life Assurance Society* (7). The case *In re Turner Morrison & Co., Ltd.* (8) does not apply to the first question, because it was admitted that the receipt there in question was income; the contest there was whether the receipt was exempt under section 4, sub-section (*3*) (*vii*). It is submitted that the judgment was incorrect in distinguishing between "arising from business" and "profits of business."

Dunne K. C., in reply. The appellant relies upon the reasoning of the concluding part of the judgment last mentioned (9). Further, if the compensation was not income, it was a "gain" within the meaning of section 6 of the Act.

(1) (1924) 9 Tax Cas. 48, 61.
(2) [1921] 2 A.C. 171.
(3) [1922] 1 K.B. 347, 358.
(4) (1920) 252 U.S. 189.
(5) [1932] 1 K.B. 124.
(6) [1891] A.C. 531, 573, 574.
(7) [1897] A.C. 647, 652.
(8) (1928) I.L.R. 56 Calc. 211.
(9) (1928) I.L.R. 56 Calc. 211, 216.

The judgment of their Lordships was delivered by

SIR GEORGE LOWNDES. This is an appeal from a judgment of the High Court at Calcutta delivered on a reference made to it under section 66 of the Indian Income-tax Act, XI of 1922. The reference arose out of an assessment to income-tax upon the respondents for the year 1929-30, in respect of an item of Rs. 9,83,361, part of a larger sum of Rs. 15,25,000 received by them in 1928 as compensation for the termination of certain agencies.

The respondents carry on business in Calcutta as merchants and agents of various companies, and have branch offices in different parts of India. For a number of years prior to 1928, they acted as distributing agents in India of the Burma Oil Company and the Anglo-Persian Oil Company, but had no formal agreement with either company. In or about the year 1927, the two companies combined and decided to make other arrangements for the distribution of their products. The respondents' agency of the Burma Company was, accordingly, terminated on the 31st December, 1927, and that of the Anglo-Persian Company on the 30th June following. Some time in the early part of 1928, the Burma Company paid to the respondents a sum of Rs. 12,00,000 "as full compensation for cessation of "the agency," and, in August of the same year, the Anglo-Persian Company paid them another sum of Rs. 3,25,000 as "compensation for the loss of your "office as agents to the company." The quotations are from letters by which the payments were recorded, and are accepted on both sides as correctly expressing the nature of the transactions.

The income-tax officer, in computing the assessable income of the respondents for the relevant year, took these two receipts into account as profits or gains of their business in the year ending the 31st December, 1928, but allowed certain deductions therefrom in respect of compensation paid by the respondents to

1932

Commissioner of Income-tax, Bengal
v.
Shaw, Wallace and Company.

various employees, leaving a balance of Rs. 9,83,361 which he included in the total income of the respondents found assessable for the year 1929-30.

The respondents objected to the assessment, and appealed to the Assistant Commissioner, who confirmed the assessment. Thereafter, on the requisition of the respondents, the Commissioner drew up a statement of the case, and referred the questions of law therein set out to the High Court with his own opinion thereon, which was against the contentions of the respondents.

The questions so formulated were as follows:—

(*a*) Was not the sum of Rs. 9,83,361, which had been included in the total income of the assessees for purposes of assessment for 1929-30, in the nature of a capital receipt and, therefore, not income, profits or gains within the meaning of the Income-tax Act ?

(*b*) If it could be said to be income, profits or gains within the meaning of the Act, was it liable to be assessed under either of the sections 10 and 12 of the Act, inasmuch as (1) it was not the profits, or gains of any business carried on by the assessees within the meaning of section 10 of the Act, nor (2) income, profits or gains from other sources within the meaning of section 12 of the Act ?

(*c*) In the alternative, was not the payment of Rs. 9,83,361 an *ex gratia* payment in the nature of a present from the oil companies in question and was it not therefore exempt under section 4 (3) (*vii*) of the Act ?

The reference was heard by the Chief Justice sitting with C. C. Ghose and Buckland JJ. The judgment of the High Court was delivered by the Chief Justice, his colleagues concurring.

The learned Judges appear to have returned a formal answer only to question (*a*), which the Chief Justice stated to be "the real question in the case." He thought that if the respondents could not escape by reason of the contention raised by this question, they must fail. The other questions, he thought, fell within a recent decision of the Court in the case of *In re Turner Morrison & Co., Ltd.* (1); he had nothing to add to what was then said on these points.

(1) (1928) I.L.R. 56 Calc. 211.

Their Lordships agree that the real matter for decision falls under (*a*), but they think that this question is not happily worded, as it seems to suggest that it was only if the sum there referred to was "in "the nature of a capital receipt" that it would be exempt from assessment, whereas the more correct proposition would seem to be that it was only if it was in the nature of an income receipt that it would fall to be assessed to the tax. The question was, however, re-stated, by the learned Chief Justice in more precise terms, *viz.*, "whether these sums are "income, profits or gains within the meaning of the "Act at all," and for the reasons stated in his judgment he came to the conclusion that they were not. Their Lordships think that his conclusion was right, though they arrive at this result by a slightly different road.

In one part of his judgment, the Chief Justice seems to hold that the "compensation for loss of these "agencies is a receipt in respect of a capital asset in "the nature of goodwill," but it has been objected with some force that there is nothing upon which this finding can be based. There was, so far as the facts disclose, no transfer of the goodwill of the respondents, and no agreement by them not to compete with the new selling agency of the companies.

In another part of the judgment the payment seems to be regarded as in the nature of compensation in lieu of notice. But here again their Lordships think that there are no facts to support such a conclusion, and they doubt if section 206 of the Indian Contract Act, upon which reliance is placed, has any application.

Again their Lordships would discard altogether the case-law which has been so painfully evolved in the construction of the English income-tax statutes—both the cases upon which the High Court relied and the flood of other decisions which has been let loose in this Board. The Indian Act is not *in pari*

1932

Commissioner of Income-tax, Bengal
v.
Shaw, Wallace and Company.

materia; it is less elaborate in many ways, subject to fewer refinements, and in arrangement and language it differs greatly from the provisions with which the courts in this country have had to deal. Under such conditions their Lordships think that little can be gained by attempting to reason from one to the other, at all events in the present case in which they think that the solution of the problem lies very near the surface of the Act, and depends mainly on general considerations.

The object of the Indian Act is to tax "income," a term which it does not define. It is expanded, no doubt, into "income, profits and gains," but the expansion is more a matter of words than of substance. Income, their Lordships think, in this Act, connotes a periodical monetary return "coming "in" with some sort of regularity, or expected regularity, from definite sources. The source is not necessarily one which is expected to be continuously productive, but it must be one whose object is the production of a definite return, excluding anything in the nature of a mere windfall. Thus income has been likened pictorially to the fruit of a tree, or the crop of a field. It is essentially the produce of something, which is often loosely spoken of as "capital." But capital, though possibly the source in the case of income from securities, is in most cases hardly more than an element in the process of production.

The sources from which the taxable income under the Act are to be derived are enumerated in section 6, which runs as follows:—

> Save as otherwise provided by this Act, the following heads of income, profits and gains, shall be chargeable to income-tax in the manner hereinafter appearing, namely:—
>
> (*i*) Salaries.
> (*ii*) Interest on securities.
> (*iii*) Property.
> (*iv*) Business.
> (*v*) Professional earnings.
> (*vi*) Other sources.

1932

Commissioner of Income-tax, Bengal
v.
Shaw, Wallace and Company.

The claim of the taxing authorities is that the sum in question is chargeable under head (*iv*), business. By section 2 (*4*) business "includes any trade, "commerce or manufacture, or any adventure or "concern in the nature of trade, commerce or "manufacture." The words used are no doubt wide, but underlying each of them is the fundamental idea of the continuous exercise of an activity. Under section 10, the tax is to be payable by an assessee under the head business "in respect of the profits or "gains of any business *carried on by him.*" Again, their Lordships think, the same central idea: the words italicised, are an essential constituent of that which is to produce the taxable income: it is to be the profit earned by a process of production. And this is borne out by the provision for allowances which follows. They include rent paid for the premises where the business is carried on; the cost of current repairs in respect of such premises; interest on money borrowed for carrying on the business, *etc.*

Some reliance has been placed in argument upon section 4 (*3*) (*v*), which appears to suggest that the word "income" in this Act may have a wider significance than would ordinarily be attributed to it. The sub-section says that the Act "shall not "apply to the following classes of *income*," and in the category that follows, clause (*v*) runs:—

> Any capital sum received in commutation of the whole or a portion of a pension, or in the nature of consolidated compensation for death or injuries, or in payment of any insurance policy, or as the accumulated balance at the credit of a subscriber to any such Provident Fund.

Their Lordships do not think that any of these sums, apart from their exemption, could be regarded in any scheme of taxation as income, and they think that the clause must be due to the over anxiety of the draftsman to make this clear beyond possibility of doubt. They cannot construe it as enlarging the word "income" so as to include receipts of any kind which are not specially exempted. They do not think that the clause is of any assistance to the appellant.

1932

Commissioner of Income-tax, Bengal
v.
Shaw, Wallace and Company.

Following the line of reasoning above indicated, the sums, which the appellant seeks to charge can, in their Lordships' opinion, only be taxable if they are the produce, or the result, of carrying on the agencies of the oil companies in the year in which they were received by the respondents. But when once it is admitted that they were sums received, not for carrying on this business, but as some sort of *solatium* for its compulsory cessation, the answer seems fairly plain.

If the business had been sold—even if that somewhat indeterminate asset known as the "goodwill" had been assigned to the employing companies, as the High Court seems to have thought it had—it is conceded that the price paid would not have been taxable. But why? Plainly because it could not be regarded as profit or gain from carrying on the business, and their Lordships think that the same reasoning must apply when the sum received is in the nature of a *solatium* for cessation.

It is contended for the appellant that the "business" of the respondents did in fact go on throughout the year, and this is no doubt true in a sense. They had other independent commercial interests which they continued to pursue, and the profits of which have been taxed in the ordinary course without objection on their part. But it is clear that the sum in question in this appeal had no connection with the continuance of the respondents' other business. The profits earned by them in 1928 were the fruit of a different tree, the crop of a different field.

For the reasons given, their Lordships are of opinion that question (*a*) was rightly answered by the High Court in favour of the assessee. No objection has been taken to the form of the answer or to its sufficiency, and it would seem unnecessary therefore to deal with the other two questions. Their Lordships will only add that the reasoning of this

1932

Commissioner of Income-tax, Bengal
v.
Shaw, Wallace and Company.

judgment would apply equally if the appellant based his claim on head (*vi*) "other sources" and the corresponding provisions of section 12.

With regard to the claim to exemption under section 4 (*3*) (*vii*), their Lordships think that the decision in the case of *In re Turner Morrison & Co., Ltd.* (1), to which reference has been made above, may need re-consideration in the light of this judgment. In their Lordships' view, the expression "receipts arising from business" in that clause must mean receipts arising from the carrying on of business.

Their Lordships will humbly advise His Majesty that this appeal should be dismissed with costs.

Solicitor for appellant: *Solicitor, India Office.*

Solicitors for respondents: *Linklaters & Paines.*

A. M. T.

(1) (1928) I. L. R. 56 Calc. 211.