"Any law of the State enacted not more than eighteen months before the commencement of this Constitution may within three months from such commencement be submitted to the President for his certification; and thereupon, if the President by public notification so certifies, it shall not be called in question in any court on the ground that it contravenes the provisions of clause (2) of this article or has contravened the provisions of sub-section (2) of section 299 of the Government of India Act, 1935."

It is not disputed that the Madras Act XXVI of 1948 does fulfil all the requirements mentioned above. Consequently, it is not possible for us to allow the appellants to raise the contentions which the learned counsel on their behalf wants to raise. The result is that the appeals would stand dismissed, but in the circumstances of this case we shall make no order as to costs.

Appeals dismissed.

Agent for the appellants: *S. Subramanian.*

Agent for the respondents: *R. H. Dhebar.*

THE LIQUIDATORS OF PURSA LIMITED

v.

COMMISSIONER OF INCOME-TAX, BIHAR.

1954

February 9.

[MEHR CHAND MAHAJAN C.J., S. R. DAS, GHULAM HASAN and JAGANNADHADAS JJ.]

Income-tax Act (XI of 1922) s. 10(2) (vii) proviso 2—Any such machinery or plant must have been used in the accounting year—Section 66—Finding of fact—When appeal court can intervene.

The fundamental idea underlying the words used in the definition of "business" in s. 2(4) of the Income-tax Act is the continuous exercise of an activity and the same central idea is implicit in the words "carried on by him" occurring in s. 10(1) and those critical words are an essential constituent of that which is to be produce the taxable income, and therefore the

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tax is payable only in respect of the profits or gains of the business which is carried on by the assessee.

That under clause (vii) of s. 10(2) the machinery and plant must be such as were used at least for a part of the accounting year. As the machinery and plant of the sugar factory which were sold had not at all been used for the purpose of business during the accounting year, the second proviso to s. 10 (2) (vii) could have no application and the assessees were not liable.

Although the High Court will not disturb or go behind a finding of fact of the Tribunal, it is well settled that where it is competent for a Tribunal to make findings of fact which are excluded from review, the appeal court has always jurisdiction to intervene if it appears either that the Tribunal has misunderstood the statutory language because the proper construction of the statutory language is a matter of law or that the Tribunal has made a finding for which there is no evidence or which is inconsistent with the evidence and contradictory of it.

Commissioner of Income-tax v. *Shaw Wallace and Company* (L.R. 59 I.A. 206), and *Commissioners of Inland Revenue* v. *Fraser* (24 Tax Cases 498) referred to.

CIVIL APPELLATE JURISDICTION : Civil Appeal No. 33 of 1953.

Appeal by special leave from the Judgment and Order dated the 16th May, 1951, of the High Court of Judicature at Patna in Miscellaneous Judicial Case No. 126 of 1950, arising out of the Order dated the 17th May, 1949, of the Income-tax Appellate Tribunal, Calcutta Bench, Calcutta, in I.T.A. No. 147 of 1948-49.

Sukumar Mitra (*S. N. Mukherjee,* with him) for the appellant.

C. K. Daphtary,. Solicitor-General for India (*Porus A. Mehta,* with him) for the respondent.

1954. February 9. The Judgment of the Court was delivered by

DAS J.—This is an appeal by special leave from the judgment of the Patna High Court delivered on a reference made by the Income-tax Appellate Tribunal under section 66(1) of the Indian Income-tax Act.

The tribunal referred the following two questions for the opinion of the High Court :

1. On the facts and in the circumstances of this case is the surplus of Rs. 13,05,144 arising out of the sale of the plant and machinery of the sugar factory chargeable under section 10 (2) (vii) ?

2. Was the profit of Rs. 15,882 on the sale of stores of the factory taxable under the Income-tax Act in the circumstances of this case ?

The reference came up for hearing before a Division Bench consisting of Shearer and Sarjoo Prasad JJ. and after a prolonged hearing the learned Judges delivered separate judgments on the 27th February, 1951, giving divergent answers to the questions, Shearer J. answering both the questions in the negative and Sarjoo Prasad J. giving an affirmative answer to both of them. The matter thereupon was placed before a third Judge, Ramaswami J., who, after a fresh hearing delivered his judgment on the 16th May, 1951, agreeing with Sarjoo Prasad J. on the first question and with Shearer J. on the second question. The result was that the High Court by a majority decision answered the first question in the affirmative, *i.e.,* against the assessee, and the second question in the negative, *i.e.,* in favour of the assessee.

The assessee applied to the High Court for leave to appeal to this court against the High Court's decision on the first question. The High Court having declined to grant the necessary certificate the assessee applied for and obtained the special leave of this court to prefer the present appeal. The department has not preferred any appeal against the High Court's decision on the second question and nothing further need be said about that question.

The controversy arose in course of the proceedings for the assessment of Pursa Ltd., to income-tax for the assessment year 1945-46, the relevant accounting year covering the period between the 1st October, 1943, to 30th September, 1944. Pursa Ltd., was a company incorporated in 1905 under the Indian Companies Act but all its shareholders and directors were residents in the United Kingdom. The business of the

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company was that of growers of sugarcane, manufacturers of sugar and dealers in sugar. It is common ground that the crushing season for the manufacture of sugar is from December to April of each year. It appears that towards the end of 1942 an attempt was made to sell the entire business of the company but such attempt did not succeed. It appears from the case filed by the respondent in this appeal that in the middle of 1943 the directors of the company commenced negotiations for the sale of the factory and other assets of the company with the ultimate object of winding up the company. From the correspondence, affidavit and other materials placed before the tribunal and referred to by Sarjoo Prasad J. in his judgment it appears that on the 9th August, 1943, an inventory was prepared and a firm offer was received from Dalmia Jain & Company Ltd., for the purchase of the factory and stores as on that date. This offer was on the 16th August, 1943, communicated by cable to the directors in England. On the 20th August, 1943, the directors asked the local managers in India to proceed with the matter in anticipation of the sanction of the shareholders which the directors expected to obtain at an extraordinary general meeting to be held very shortly. That meeting, however, was held on the 8th October, 1943, *i.e.*, 8 days after the accounting year had started. At that meeting the firm offer of Dalmia Jain & Company Ltd. was accepted and a concluded agreement for sale came into existence. Thereafter instructions were given to the solicitors to draw up the necessary documents.

On the 7th December, 1943, a written memorandum of agreement was executed whereby the company agreed to sell and demise to Dalmia Jain & Company Ltd., free from all mortgages and charges at and for the price of rupees twenty-eight lacs all the lands, buildings, machinery and plant and all vats, reservoirs, cisterns, pumps, machinery, engines, boilers, plant, implements, utensils, tramways, furniture, stores, articles and things as on the ninth day of August, one thousand nine hundred and forty-three (subject to subsequent use and consumption in the ordinary course

of business) used in connection with the said sugar factory, but excepting stocks of manufactured sugar and stocks of grain in godown on the ninth day of August, one thousand nine hundred and forty-three and all stores and other articles bought or received by the company after the date. Dalmia Jain & Company Ltd., paid the sum of rupees twenty-eight lacs on the same day and on the 10th December, 1943, they got possession of the factory. On the date of the aforesaid sale, the company possessed sugar stock valued at rupees six lacs which was excluded from the sale. This stock of sugar the company continued to sell up to June, 1944. It is said that the said stock of sugar was excluded because at the time it was not possible to know at what date such a sale would be concluded and the sugar produced in 1943 had to be sold by and through the exclusive selling agents of the company under a contract entered into with them. It is, however, not disputed that between the 9th August, 1943, when the firm offer was obtained and the 10th December, 1943, when possession of the factory was made over to Dalmia Jain & Company Ltd., the company never used the machinery and plant for the purpose of manufacturing sugar or for any other purpose except that of keeping them in trim and running order. Indeed, throughout the accounting period the machinery and plant were not used by the company.

The company went into voluntary liquidation on the 20th June, 1945. The reason for the delay in putting the company into liquidation is said to have been caused by considerable legal difficulties with regard to the transfer of certain *mokarari* lands belonging to the company. The liquidators appointed by the shareholders of the company represented the company in the matter of proceedings for assessment of the company for the assessment year 1945-46.

In the course of these assessment proceedings the Income-tax Officer on the 21st February, 1947, wrote a letter to the liquidators asking for elucidation on certain points. Amongst other things, the Income-tax Officer wanted to know the liquidators' objection why the company's activities during the previous

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year might not be treated as amounting to a realisation of assets on impending liquidation rather than to the carrying on of business within the meaning of the Income-tax Act. To this letter an answer was sent by the liquidators on the 19th March, 1947, pointing out that the company had gone into liquidation on the 20th June, 1945, and that in view of the date of liquidation the liquidators could not agree that the company was not carrying on business during the year ended 30th September, 1944, and they further pointed out that the various debits contained in the sugar factory accounts were those incurred in carrying on the company's business. By his letter dated the 17th May, 1947, the Income-tax Officer claimed that large profits which had been made by the company on the sale of their machinery and plant were taxable under the second proviso to section 10 (2) (vii) of the Income-tax Act and called upon the liquidators to retain sufficient funds and assets in their hands to meet the heavy tax liabilities that might eventually arise and also to warn the shareholders accordingly. He also asked for certain information which, however, the liquidators did not furnish. The liquidators, in their letter in reply dated the 22nd May, 1947, did not agree that the profits were taxable, for the profits to which reference had been made were not profits arising from a business carried on by the company but were profits arising from the company ceasing to carry on business. The Income-tax Officer, however, by his order dated the 21st June, 1947, held that the profits of the sale of machinery and plant were liable to assessment under section 10 (2) (vii) of the Act and added a sum of Rs. 13,05,144 to the profits.

The Appellate Assistant Commissioner of Income-tax having dismissed the liquidators' appeal on the 30th January, 1947, the liquidators went up on further appeal to the Income-tax Appellate Tribunal. By its order dated the 17th May, 1949, the tribunal dismissed that appeal. Upon an application under section 66(1) of the Act the tribunal stated a case to the High Court referring the two questions hereinbefore

set out. The subsequent history of the matter has already been mentioned and needs no reiteration.

The relevant portion of section 10 of the Income-tax Act as amended by Act VI of 1939 was as follows :—

"10 (1) The tax shall be payable by an assessee under the head "Profits and gains of business, profession or vocation" in respect of the profits or gains of any business, profession or vocation carried on by him.

(2) Such profits or gains shall be computed after making the following allowances, namely :—

(i).....

(ii).....

(iii).....

(iv) in respect of insurance against risk of damage or destruction of buildings, machinery, plaint, furniture, stocks or stores, used for the purposes of the business, profession or vocation, the amount of any premium paid ;

(v) in respect of current repairs to *such* buildings, machinery, plant, or furniture, the amount paid on account thereof ;

(vi) in respect of depreciation of *such* buildings, machinery, plant, or furniture being the property of the assessee, a sum equivalent to such percentage on the original cost thereof to the assessee as may in any case or class of cases be prescribed :

.....

(vii) in respect of *any* machinery or plant which has been sold or discarded, the amount by which the written down value of the machinery or plant exceeds the amount for which the machinery or plant is actually sold or its scrap value :

Provided that such amount is actually written off in the books of the assessee :

Provided further that where the amount for which any *such* machinery or plant is sold exceeds the written down value, the excess shall be deemed to be profits of the previous year in which the sale took place ;

.....

....."

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It is necessary to bear in mind the meaning and import of the provisions of section 10 (2) (vii) in so far as they apply to the present case.

Under section 10 tax is payable by an assessee "in respect of the profits or gains of any business, profession or vocation carried on by him." "Business" is defined by section 2, sub-section (4) as "including any trade, commerce or manufacture, or any adventure or concern in the nature of trade, commerce or manufacture." As pointed out by the Judicial Committee in *Shaw Wallace & Co.'s* case([1]) the fundamental idea underlying each of these words is the continuous exercise of an activity and the same central idea is implicit in the words "carried on by him" occurring in section 10 (1) and those critical words are an essential constituent of that which is to produce the taxable income. Therefore, it is clear that the tax is payable only in respect of the profits or gains of the business which is carried on by the assessee. Sub-section (2) permits allowances to be made before the taxable profits are ascertained. Proviso (2) to clause (vii) of that sub-section on which the Income-tax authorities have relied makes the excess of sale proceeds over the written down value of "any *such* machinery or plant" to be deemed to be profits of the previous year in which the sale took place. Any *such* machinery or plant in the proviso clearly refers to the machinery or plant in respect of which the allowance is to be given under that clause. Although the word "such" was not used in the body of clause (vii), the scheme of sub-section (2) which is apparent from the other clauses of allowances *e.g.*, (iv), (v) and (vi), clearly indicates that the machinery or plant referred to in clause (vii) must be the same as those mentioned in the earlier clauses, *i.e., such* machinery or plant as were "used for the purposes of the business, profession or vacation." Indeed, the position has been made clear and placed beyond any doubt by the subsequent amendment of 1946 which added the word "such" in clause (vii). The words "used for the purposes of the business" obviously

[1] L. R. 59 I.A. 206 at P. 213.

mean used for the purpose of enabling the owner to carry on the business and earn profits in the business. In other words, the machinery or plant must be used for the purpose of that business which is actually carried on and the profits of which are assessable under section 10 (1). The word "used" has been read in some of the pool cases in a wide sense so as to include a passive as well as active user. It is not necessary, for the purposes of the present appeal, to express any opinion on that point on which the High Courts have expressed different views. It is, however, clear that in order to attract the operation of clauses (v), (vi) and (vii) the machinery and plant must be such as were used, in whatever sense that word is taken, at least for a part of the accounting year. If the machinery and plant have not at all been used at any time during the accounting year no allowance can be claimed under clause (vii) in respect of them and the second proviso also does not come into operation.

In its statement of the case, after referring to its decision that the profits on the sale of machinery and plant were assessable under section 10 (2) (vii), the tribunal proceeded to state :

"This decision was based on two considerations. First, that as admitted by the applicant company the company had been carrying on its business up to the date of the sale of the machinery, namely, 7th December, 1943. The tribunal was of the opinion that as the applicant company had not ceased to carry on its business till the date of the sale of the machinery, it must be held that the sale of the machinery was a part of the applicant company's carrying on of the business. The second reason for the decision of the tribunal was that the applicant company did not sell its sugar stocks amounting to over Rs. 6,00,000 on 7th December, 1943. The applicant company's plea that the sugar stocks could not be sold as the applicant company had sole agents for the sale of sugar, was not accepted by the tribunal. The Income-tax Appellate Tribunal found that sugar continued to be sold for more than 6 months

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after the sale of the machinery and substantial expenses on establishment and general charges continued to be incurred. From this the Income-tax Appellate Tribunal concluded that the sugar stocks had not been sold on 7th December, 1943, purposely in order to sell these to the best advantage later on. This, the Income-tax Appellate Tribunal held, showed that the applicant company carried on business even subsequent to the sale of machinery on 7th December, 1943."

Although the High Court will not disturb or go behind the finding of fact of the tribunal, it is now well settled that where it is competent for a tribunal to make findings in fact which are excluded from review, the appeal court has always jurisdiction to intervene if it appears either that the tribunal has misunderstood the statutory language—because the proper construction of the statutory language is a matter of law—or that the tribunal has made a finding for which there is no evidence or which is inconsistent with the evidence and contradictory of it. [See Lord Normand in *Commissioners of Inland Revenue* v. *Fraser*(1)]. It appears to us that the tribunal misdirected itself in law as to the meaning and import of the relevant provisions of section 10 of the Act. It completely overlooked the fact which is plainly in evidence on the record that the machinery and plant which were sold had not at all been used for the purposes of the business carried on in the accounting year and consequently the second proviso to section 10 (2) (vii) could have no application to the sale proceeds of such machinery and plant. In fact the entire decision of the tribunal was vitiated by its failure to keep in view the true meaning and scope of section 10 (2) (vii) and cannot, therefore, be supported.

It further appears to us that in the statement of the case the tribunal was not merely stating something in the nature of a primary fact but was also drawing a conclusion which is to a certain extent contrary to the primary finding. As is stated clearly in the statement of the case, the decision of the tribunal was based on

(1) 24 Tax Cas. 498 at p. 501.

two considerations. The first consideration was founded on an admission by the liquidators that the company had been carrying on its business up to the date of the sale of the machinery on the 7th December, 1943. This admission is quite consistent with the case that the company was only selling its stock of sugar and not doing any business of manufacture of sugar. Indeed, the manufacturing process does not begin until December of each year and the memorandum of agreement was made on the 7th December, 1943, and possession was delivered to the purchaser on the 10th December, 1943. It is nobody's case and it has not been found that the company had manufactured any sugar during the whole of the accounting year. Therefore, this finding that the company carried on its business up to the 7th December, 1943, certainly does not indicate that the company was also carrying on any business of growing sugarcane or manufacturing sugar by the use of the machinery or plant in question. The second finding that the company carried on business even after the sale of the machinery and the plant clearly indicates that that business had nothing to do with the machinery or plant. Both the findings, therefore, are inconclusive. The matter, however, does not rest there. It appears to us that the findings of fact, taken literally, cannot support the decision of the tribunal. If, as held by the tribunal, "the sale of the machinery was a part of the applicant company's carrying on of the business" then the sale must be regarded as an ordinary operation of such business and consequently the profits arising out of such ordinary business operation would be assessable under the provisions of section 10 (1) and it would not be necessary to have recourse to the statutory fiction created by the second proviso to clause (vii) under which the excess of the sale proceeds over the written down value is to be deemed to be profits of the business. If the profits on the sale of the machinery and plant are to be made assessable under the second proviso, as has been done by the tribunal, then it must be conceded that these deemed profits were not in reality the profits of the business carried on by the

(2) 24 Tax Cases 498 at p. 501.

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company and, therefore, the sale transaction which brought in these profits was not in fact part of the company's business, which conclusion again will be inconsistent with the finding of fact if the business is not understood as limited only to the selling of sugar.

For reasons stated above, it appears to us that having misdirected itself in law as to the scope and effect of the relevant portions of section 10 of the Act the tribunal did not approach the facts from a proper angle and, further, that its findings cannot, in the circumstances of this case, be given such sanctity as would exclude the same from review by the High Court or this court. Turning to the facts to be gathered from the records it is quite clear that the intention of the company was to discontinue its business and the sale of the machinery and plant was a step in the process of the winding up of its business. The sale of the machinery and plant was not an operation in furtherance of the business carried on by the company but was a realisation of its assets in the process of gradual winding up of its business which eventually culminated in the voluntary liquidation of the company. Even if the sale of the stock of sugar be regarded as carrying on of business by the company and not a realisation of its assets with a view to winding up, the machinery or plant not being used during the accounting year at all and in any event not having had any connection with the carrying on of that limited business during the accounting year, section 10 (2) (vii) can have no application to the sale of any such machinery or plant. In this view of the matter, the answer to the first question should be in the negative and we answer accordingly.

The result is that this appeal is allowed and the respondent shall pay the costs of the appellants both in this court and in the High Court.

Appeal allowed.

Agent for the appellant : *B. N. Ghose.*

Agent for the respondent : *G. H. Rajadhyaksha.*