Privy Council Appeal No. 89 *of* 1932.
Allahabad Appeal No. 2 *of* 1932.

The Commissioner of Income Tax, United Provinces of Agra and Oudh - - - - - - - - - *Appellant*

v.

Tehri-Garhwal State, through Ram Prasad, principal officer - *Respondent*

FROM

THE HIGH COURT OF JUDICATURE AT ALLAHABAD.

JUDGMENT OF THE LORDS OF THE JUDICIAL COMMITTEE OF THE PRIVY COUNCIL, DELIVERED THE 1ST DECEMBER, 1933.

Present at the Hearing:

LORD MACMILLAN.
SIR JOHN WALLIS.
SIR GEORGE LOWNDES.

[*Delivered by* SIR GEORGE LOWNDES.]

Between the 1st April, 1925, and the 31st March, 1926, the Tehri-Garhwal State, the respondent in this appeal, carried on a timber business in British India, which resulted in considerable profits. The State was not during that year subject to the Indian Income Tax Law, but in 1926 the Government Trading Taxation Act was passed by the Indian Legislature and came into force on the 1st April that year. Section 2 of the Act is in the following terms :—

> 2.—(1) Where a trade or business of any kind is carried on by or on behalf of the Government of any part of His Majesty's Dominions, exclusive of British India, that Government shall, in respect of the trade or business and of all operations connected therewith, all property occupied in British India, and all goods owned in British India for the purposes thereof, and all income arising in connection therewith, be liable—
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> (*a*) to taxation under the Indian Income Tax Act, 1922, in the same manner, and to the same extent as in the like case a company would be liable ;

(*b*) to all other taxation for the time being in force in British India in the same manner as in the like case any other person would be liable.

(2) For the purposes of the levy and collection of income tax under the Indian Income Tax Act, 1922, in accordance with the provisions of subsection (1), any Government to which that subsection applies shall be deemed to be a company within the meaning of that Act, and the provisions of that Act shall apply accordingly.

(3) In this section the expression " His Majesty's Dominions " includes any territory which is under His Majesty's protection or in respect of which a mandate is being exercised by the Government of any part of His Majesty's Dominions.

Assuming for the purposes of the present appeal that under this section the State became (as has been held in India) liable to taxation for the revenue year 1926–7 upon the profits of its timber business, income tax would be chargeable under Section 3 of the Act of 1922 *in respect of* its trading profits for the previous year, *i.e.*, the year ending the 31st March, 1926, and super-tax would follow under Section 55, at the rates imposed by the Finance Act for the year.

The State was accordingly in the year 1926 called upon to pay by way of income tax and super-tax sums totalling Rs. 43,294–14–0, calculated upon the profits earned in 1925–6. The figures are not now in dispute, but from the first the State has contested its liability to taxation. It appealed from the original assessing authority to the Commissioner, and from the Commissioner, upon a reference made by him under Section 66 (2) of the Act, to the High Court.

This reference was heard by Mukerji and Niamatullah JJ. on the 21st November, 1929. Four questions of law had been formulated by the Commissioner. Question (1) was upon the State's contention that the Act of 1926 was not applicable to it. Questions (3) and (4) were concerned with the nature of its dealings in British India. Question (2), upon the answer to which their Lordships think that the result of the present appeal depends, was as follows :—

(2) Whether, since the Government Trading Taxation Act only came into force on the 1st April, 1926, there is any liability for assessment with reference to transactions which took place before that date ?

Upon this question the judgment of the High Court must be quoted in full :—

" Now we come to Question 2. The argument is that the income that is being taken into consideration, for taxation accrued to the State in 1925–26, that the Government Trading Taxation Act came into force on 1st April, 1926, and that, therefore, it would have no application to the income which was earned in the previous year (1925–26). On the face of it, this argument is very attractive ; but in view of the language employed in Section 3 of the Indian Income Tax Act we do not think that it has much force. The Tehri State, we have been told, has continued this business in years subsequent to 1925–26, and the Income Tax Department has sought to assess it for the year 1926–27. The tax is to be paid in and for that year. The Income Tax Department is armed with power to tax the Tehri State any

time after 1st April, 1926. That being so, let us read Section 3 of Act XI of 1922. We have already read it once before. Now, substituting the years with which we have to deal, the section would read as follows :—

> ' Where any Act of the Indian Legislature enacts that income tax shall be charged for the year 1926–27 . . . tax, . . . shall be charged for the year 1926–27 . . . in respect of all the income, profits and gains of the previous year (1925–26). . . .'

" This is the natural reading of Section 3 in view of the facts before us. It seems to be quite clear to us that the tax which has to be paid by the Tehri State for the year 1926–27 is to be paid on the amount of profits earned by it in the year 1925–26. If the State decided to stop its business, say, in the year 1930–31, the tax paid by it in 1930–31, on the basis of the income of 1929–30, would be liable to be refunded, in so far as the income of the year 1930–31 fell short of the income earned in 1929–30."

In the result the learned Judges were of opinion that none of the grounds taken by the State were tenable.

By the time this judgment was delivered it had apparently been ascertained that the State had in fact no taxable income in the year 1926–7, though whether the business had been discontinued, as the High Court seems to think, or whether it was only that no profits resulted, seems to be uncertain.

A part payment of Rs. 25,000 had been made by the State before the reference, which left a balance of Rs. 18,294–14 due upon the demand of the income tax authorities. The State, basing itself upon the judgment of the High Court, claimed the return of the Rs. 25,000 on the ground that it had no taxable income in the year 1926–7. The Commissioner with equal confidence claimed payment of the Rs. 18,294–14–0. A second reference was thereupon made to the High Court, this time by the Commissioner of his own motion, asking for the determination of the following questions :—

" (1) Does the judgment delivered by the High Court in miscellaneous case No. 671 of 1929 on 21st November, 1929, operate of its own force to require the Income Tax Department to refund the sum of Rs. 25,000 paid by the Tehri Darbar, and to refrain from collecting the balance of Rs. 18,294–14–0 ?

" (2) If the answer to Question (1) is in the negative :—

" (*a*) Is the Tehri Darbar liable to pay the balance of Rs. 18,294–14–0 ?

" (*b*) Is the Tehri Darbar entitled to a refund of the amount already paid, *i.e.*, Rs. 25,000 ? "

The reference was heard by the same two Judges as in the previous case, and their judgment was delivered in the 6th November, 1931. They answered the first question in the affirmative, and held that the State was not liable to pay the balance of Rs. 18,294–14–0, and that it was entitled to a refund of the Rs. 25,000.

The learned Judges recited the passage from their previous judgment, which has been quoted above, and proceeded to

interpret the language they had used, and the principle upon which their decision was based. They said :—

> " We have carefully read our order of [November 21st, 1929] and entertain no doubt as to what we intended to hold and did hold. On a consideration of Section 2 of the Government Taxation Act (III of 1926), we were quite clear that the liability of the Tehri State to pay the income tax arose for the first time after the 1st April, 1926, if it had assessable income in British India after that date. We proceeded to hold that the Tehri State was liable to pay income tax on the income of 1926–27 which, for the purposes of assessment, was to be measured by the income received in the preceding year (1925–26). We did not intend to hold and did not hold, nor is there anything to that effect in our order, dated 21st November, 1929, that the Tehri State was liable to pay income tax on the income received before the 1st April, 1926, when the liability arose, that is, in the year 1925–26, the income of which year was imported into the consideration of the case merely as the basis of provisionally ascertaining the income of 1926–27, on which the tax was demanded. It was for this reason that a reference to possible refund in some future year was made by us. It is obvious that, if the income of the current year has to be taxed, the exact amount of income cannot be ascertained before the expiry of the year and that, if the tax is assessed and collected on the basis of the income of the preceding year, the question of refund must arise in case the business is discontinued in that year,* if the total income falls short of the income of the preceding year, which was assumed for the purposes of assessment as the income of the current year. This process of reasoning and the assumption that the assessment had been made in respect of the income of 1926–27 were partly, at any rate, inspired by the view expressed in the order of the Income Tax Commissioner, dated 14th March, 1928, and by the strenuous opposition offered on behalf of the Crown to the contention of the Tehri State that the tax was claimed in respect of the income of the year 1925–26. Holding, as we did, that the Tehri State had been assessed to tax in respect of the income of 1926–27, calculated provisionally on the basis of the income which had accrued in 1925–26, we repelled the objection of the Tehri State. The provision of refund in our order in case of discontinuance of business in any future year in respect of which the tax might be assessed and collected is an integral part of our order and a necessary corollary to the rule on which we upheld the assessment then under reference. It was not an *obiter dictum.*"

No inconsistency has been pointed out between the passage here cited and that quoted from the first judgment, and their Lordships think that this must be taken to be the meaning and effect of that judgment.

The Commissioner being dissatisfied with the decision of the High Court has appealed to His Majesty in Council, asking for its reversal.

The principal contention on his behalf is that the learned Judges have misconstrued Section 3 of the Act of 1922 ; that the intention of the section is not to treat the income of the previous year merely as a measure of the unascertained income of the year of assessment, but to tax the assessee in the year of assessment upon the income received by him in the previous year,

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* *Note.*—The word " or " seems to have dropped out here.

and that this is clearly competent in the case of the Tehri-Garhwal State under the Act of 1926. It is contended that though the theory adopted by the learned Judges may have been right under the provisions of the previous Income Tax Act of 1918, a definite change of system was made by the Act of 1922, and reliance is placed in this connection upon a decision of the Calcutta High Court, *In re Beharilal Mullick*, I.L.R. 54, Calc. 630.

Their Lordships think that there is much force in these contentions, and if the question they had to decide on the present appeal were merely as to the true meaning of Section 3 of the Act of 1922, they might be prepared to endorse the view taken by the Calcutta High Court. But that is not the position in the case now before them. The former judgment of the 21st November, 1929, was not appealed against, and, whether right or wrong, must govern the relations of the parties in the particular case. It is to be noticed that under Section 66 (5) of the Act of 1922, the judgment of the High Court is to contain the grounds upon which the decision is founded: that a copy of the judgment is to be sent to the Commissioner, and that the case is to be disposed of by the income tax authorities "conformably to such judgment." Under this provision their Lordships think that the judgment as a whole is binding between the parties in the particular case. If the judgment expounded a wrong construction of the Act, as the appellant now contends, an appeal against it was open, and there is no other procedure by which it could be corrected.

On the assumption, which their Lordships are satisfied must be made for the purposes of the present appeal, that Section 3 of the Act was to be construed in the way the learned Judges construed it, they think that the consequences would follow which have been ascribed to this construction in the judgment now under appeal; that the respondent State would be relieved from the demand for payment of the Rs. 18,294–14–0, and would be entitled to repayment of the Rs. 25,000. In their opinion, therefore, the appeal fails and should be dismissed with costs, and they will humbly advise His Majesty accordingly.

In the Privy Council.

THE COMMISSIONER OF INCOME TAX, UNITED PROVINCES OF AGRA AND OUDH

v.

TEHRI-GARHWHAL STATE, THROUGH RAM PRASAD, PRINCIPAL OFFICER.

DELIVERED BY SIR GEORGE LOWNDES.

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