
(1969) 07 CAL CK 0033

In the Calcutta High Court

Case No : Income-tax Reference No. 125 of 1967

Daulatram Rawatmull

APPELLANT

Vs

Commissioner of Income Tax (Central)

RESPONDENT

Date of Decision : 01-07-1969

Acts Referred:

Income Tax Act, 1922 — Section 10(1), 10(2), 24(1)

Citation : (1970) 78 ITR 503

Hon'ble Judges : Sankar Prasad Mitra, J;Sabyasachi Mukharji, J

Bench : Division Bench

Judgement

Sankar Prasad Mitra, J.—This reference u/s 66(1) of the Indian Income Tax Act, 1922, arises out of the assessment proceedings for the assessment year 1956-57. The relevant previous year is the Deshera year commencing on October 7, 1954, and ending on October 25, 1955. The assessee is a registered firm. Its head office is in Calcutta. It has branch in Bombay which was carrying on the business of exporting groundnut oil. The assessee had regular transactions with Messrs. N. Schrok, N. V. Rotterdam. During the relevant year the assessee fulfilled severa contracts with the Rotterdam party by making deliveries of the goods contracted for. On November 4, 1953, the assessee entered into a contract with the party at Rotterdam for delivery of 200 tons (of 2,240 lbs. each) of Indian crude groundnut oil for January and/or February, 1954, shipment at ₹125 per ton. But the assessee could not secure the export licence for shipping the goods. On the date of the contract the Government of India had not announced its export policy but during the first half of the year exports were normally permitted. The Tribunal observed that the assessee must have thought that by January-February, 1954, the export permit would be available and it would be able to make the supplies of the contracted goods. But the assessee's expectations were belied and it failed to supply the goods contracted for. In pursuance of the contract an arbitrator was appointed. The arbitrator gave an award on December 30, 1954, There was an appeal against this award but the award was confirmed. In the award the assessee was directed to pay the

difference between the market rate of ₹141 per ton (less 1%) and the contract rate of ₹125 per ton. In Indian money the difference came to Rs. 44,226. The assessee remitted this sum of Rs. 44,226 to the foreign party with the sanction of the Reserve Bank of India.

2. The assessee claimed deduction of the said sum of Rs. 44,226 in the assessment for the relevant year. The Income Tax Officer did not accept the claim. He held that since the contract had been settled by payment of differences, the loss was a loss in speculation falling within the scope of Explanation 2 of Section 24(1) of the Act of 1922.

3. The Appellate Assistant Commissioner confirmed the order of the Income Tax Officer. The assessee's contention before the Tribunal was that the aforesaid sum was paid by way of liquidated damages and could not be treated as a loss in speculation. The assessee submitted that it was, therefore, an expenditure allowable u/s 10(1) or Section 10(2)(xv) of the Act. The Tribunal has held that the said sum of Rs. 44,226 was rightly treated as a loss in speculation.

4. The following question has, in the circumstances, been referred to this court :

"Whether, on the facts and in the circumstances of the case, the sum of Rs. 44,226 was a loss in speculation within the meaning of Explanation 2 to Section 24(1) or an allowable expenditure u/s 10(1) or Section 10(2)(xv) of the Indian Income Tax Act, 1922?"

5. Let us, at the outset, set out the relevant provisions of Section 24, They are as follows:

"24. Set-off of loss in computing aggregate income.--(1) Where any assessee sustains a loss of profits or gains in any year under any of the heads mentioned in Section 6, he shall be entitled to have the amount of the loss set off against his income, profits or gains under any other head in that year:

Provided that in computing the profits and gains chargeable under the head "profits and gains of business, profession or vocation", any loss sustained in speculative transactions which are in the nature of a business shall not be taken into account except to the extent of the amount of profits and gains, if any, in any other business consisting of speculative transactions . . .

Explanation 2.--A speculative transaction means a transaction in which a contract for purchase and sale of any commodity including stocks and shares is periodically or ultimately settled otherwise than by the actual delivery or transfer of the commodity or scrips."

6. It would be necessary, to appreciate the contention of the department's counsel, to set out some of the clauses of the contract in the instant case. Clause 10 of the contract runs thus :

"Sellers shall provide the appropriate certificate of origin if required. If before the fulfilment of this contract, either party, whether an individual, firm or company,

shall give notice to any of his creditors that he has suspended, or that he is about to suspend payment of his debts, or shall commit an act of bankruptcy, or being a company shall be unable to pay its debts within the meaning of... of Companies Act, 1948, or have an order made, or pass resolution for . . .winding up (other than for purposes of reconstruction or amalgamation) or have a receiver appointed, the contract shall forthwith be closed at a price to be fixed by the price fixing committee appointed by the London Oil and Tallow Traders" Association. The difference between the contract price and the price so fixed shall be the amount payable or receivable under this contract. The parties shall be bound to furnish to the price committee such information and produce to the committee such books, papers and documents as are incidental to the default.

In default of fulfilment of contract by either party the other party at his discretion shall after giving notice in writing have the right to sell or purchase as the case may be against the defaulter who shall make good the loss if any on such sale or purchase on demand. If the party liable to pay shall be dissatisfied with the price of such sales or purchase or if the above rights is not exercised the damage, if any, payable by the party in default shall be settled by arbitration and such damages shall be limited to the difference between contract price and market price unless the default is caused by a wilful failure of a seller to tender documents after an appropriation has been made in which case in assessing damages arbitrators may in their absolute discretion have regard to .any loss of profit or any liability incurred by buyers under any sub-contract he may have entered into."

7. Reliance has also been placed on Clause 15 of this contract which apparently has not been correctly printed in the paper book at pages 11 and 12 thereto. The relevant portions of this clause (with the corrections) are set out below :

"Force Majeure 15. (a) In the event of war, hostilities or blockade preventing (the shipment) during the contract period, this contract or any unfulfilled part thereof shall be cancelled, (b) Should (the shipment) be delayed by fire, strikes, lock-outs, riots or revolution, prohibition of export or any executive or legislative act done by or on behalf of the Government of the territory where the port and/or ports of shipment named herein is situate or of any cause comprehended in the term "force majeure" other than the reasons given in Clause (a) the time of shipment shall be extended by two months. Should shipment not be possible within these two months the contract (is) to be void ..."

8. Mr. B.L. Pal, learned counsel for the revenue, has urged before us that each reported case on the subject deals with the construction of the relevant contract. The contract in the present case, according to Mr. Pal, was in the standard form prescribed by a well-known trade association in London. In that form, for the convenience of the contracting parties, the association made ample provision for what was to happen in the case of difficulties arising in the performance of the contract. That is why, says Mr. Pal, the association made a distinction between "default" and breach of contract. Clause 10 is the "default" clause; but the

present case can be squarely brought within clause 15 (b) which does not involve any "default" at all. In these premises, contends Mr. Pal, the arbitrator's award, in the instant reference, should be treated as an award in fulfilment of the contract itself and the transaction would come within the purview of Explanation 2 to Section 24 (1) of the Indian Income Tax Act, 1922.

9. In our view this contention of counsel for the Commissioner cannot be examined in this reference at all. The admitted facts are that in terms of the contract between the parties there has been an award and that award has also been upheld on appeal. The appointment of the arbitrator and the award of the arbitrator have been provided for in Clause 10 of this contract which is a clause dealing exclusively with "default". On these facts, this court must assume that it is a case of "default" within the meaning of Clause 10 and there is no scope for invoking any of the provisions of Clause 15. In these circumstances, the judgment of this court in COMMISSIONER OF Income Tax, WEST BENGAL Vs. PIONEER TRADING COMPANY PRIVATE LTD., appears to be relevant. It has been held that a claim based on breach of contract does not come within the meaning of "contract settled", as used in Explanation 2 to Section 24 (1) of the Indian Income Tax Act, 1922; after the breach of contract, the cause of action is no longer based on the contract itself but on its breach; where the money which the assessee received was in settlement of the amount of damages which the assessee had suffered by reason of breach of the contract to deliver, the receipt was not a receipt from a speculative transaction as defined in Explanation 2: and the money so received was not liable to be set off against speculation loss of earlier years.

10. In the light of the principles decided in this case we find in the present reference that the arbitrators were appointed in terms of the contract between the parties on the basis that the assessee committed default in fulfilment or performance of the contract; the arbitrators made an award; "there was an appeal against the award: but the award was confirmed and the assessee had to pay the damages which the arbitrators had determined. It also appears that there was no challenge to these facts before the fact finding authorities below. This is, therefore, a case not of settlement of the contract itself either periodically or ultimately, but of payment of damages for breach or non-fulfilment or non-performance of the contract. That being the case, we are of opinion, that this is not a "speculative transaction" within the meaning of Explanation 2 to Section 24 (1) of the Indian Income Tax Act, 1922,

11. Our answer to the question therefore is that the sum of Rs. 44,226 was not a loss in speculation within the scope of Explanation 2 to Section 24 (1) of the Indian Income Tax Act, 1922. No argument has been advanced before us as to whether it is allowable as an expenditure u/s 10 (1) or Section 10 (2) (xv). We, therefore, merely state that this is an allowable expenditure u/s 10 of the Act of 1922. Each party will bear and pay its own costs.