

(1968) 05 CAL CK 0044
In the Calcutta High Court
Case No : C.R. No. 1432 (W) of 1964

Deshbandhu Co-operative Powerloom Society Ltd. APPELLANT
Vs
Collector of Central Excise RESPONDENT

Date of Decision : 02-05-1968

Acts Referred:

Central Excise Rules, 1944 — Rule 2, 201, 8(1)
Central Excises and Salt Act, 1944 — Section 12, 18, 3
Criminal Procedure Code, 1898 (CrPC) — Section 165
Sea Customs Act, 1878 — Section 110, 110(3)

Citation : (1969) 2 ILR (Cal) 223

Hon'ble Judges : D. Basu, J

Bench : Single Bench

Advocate : Anil Kumar Sinha, Ambica Ch. Bhattacharyya and Goutam Prasad Chatterjee, for the Appellant; Amiya Kumar Mukherjee, for the Respondent

Judgement

BANERJEE J. - This is a reference u/s 66(1) of the Indian Income Tax Act.

The year of assessment is 1959-60, corresponding to the accounting period ending with the calendar year 1958.

The question of law referred to this court is :

"Whether, on the facts and in the circumstances of the case, the Tribunal was right in holding, that the sum of Rs. 22,627 was a speculative receipt within the meaning of Explanation 2 to the third proviso to section 24(1) of the Income Tax Act, 1922, and could not therefore be assessed as a business receipt ?"

The reference to "Explanation 2 to the third proviso to section 24(1)" is somewhat misleading. There is no third proviso to section 24(1) at present. There are only two, the first proviso having been omitted by Act XLI of 1954.

Then again, Explanation 2 is referable to the second proviso, which is now really the first proviso, because the Explanation explains the expression "speculative transaction" used in that proviso. We should, therefore, read the question in a

somewhat changed manner and instead of the words "Explanation 2 to the third proviso to section 24(1)" read "Explanation 2 to section 24(1)", in order to obviate all criticism. This was agreed upon by the learned counsel appearing for the parties.

The above question of law arises in circumstances hereinafter stated in brief. The assessee, a private limited company, entered into a contract, dated July 6, 1953, with Messrs. Iwai and Co. Ltd. of Tokyo, Japan, and agreed to supply 52,000 long tons of Indian iron ore. This contract was later on varied by mutual consent and the supply of the agreed quantity of iron ores, was split up into three parts, namely, a consignment of 24,000 long tons to be supplied by way of first delivery, thereafter a delivery of 8,000 long tons, and lastly, a delivery of 20,000 long tons. The agreed basis of payment was by an irrevocable letter of credit in pound sterling at the rate of 71 shillings per dry long ton. In terms of the contract, as varied, the assessee completed the first and the second part of the contract by consigning the full quantity of ore to be consigned under those two parts. So far as the third part of the contract was concerned, under which the assessee was to consign 20,000 long tons of iron ore, there was a quantity of 12,010 long tons only consigned and accepted by the Japanese company. Out of the third part of the contract, there remained a quantity of 7,990 long tons to be consigned by the assessee to the Japanese company. This could not be supplied - because the Japanese company defaulted in performance of their part of the contract and did not open a letter of credit as agreed upon. For breach of the contract, the assessee-company claimed from the Japanese company the difference of price for the said quantity of 7,990 long tons of iron ore, not supplied because of the default on the part of the purchasing company. The claim for difference was ultimately settled and the Japanese company agreed to pay the difference amounting to Rs. 22,627 and actually paid the same in settlement of the claim.

In the assessment year, with which we are concerned, this amount was sought to be set off against certain unabsorbed speculative loss, brought forward from earlier years, on the theory that the amount of difference obtained from the Japanese company was a speculative profit. The Income Tax Officer disallowed the claim with the following observation :

"Clearly it is in the nature of damages for non-fulfillment of contract. It is right from its inception a contract for supplying of iron ore which was partly performed and executed. There was a dispute and the claim settled not in the way speculative transactions are settled but apparently in the way disputes arising on non-fulfillment of contracts are settled, i.e., by paying damages."

The assessee appealed before the Appellate Assistant Commissioner. The Appellate Assistant Commissioner agreed with the Income Tax Officer and dismissed the appeal. Thereupon, the assessee took the matter in appeal before the Appellate Tribunal. It was contended before the Tribunal that Explanation 2 to section 24(1) of the Income Tax Act, 1922, defined what a speculative

transaction meant under the Act and the contract having been settled otherwise than by actual delivery of the commodity, it could only be a speculative transaction and accordingly the receipt, a speculative receipt. We are not concerned with the other points argued before the Tribunal, regard being had to the nature of the question referred to us. This contention was sought to be repelled on behalf of the revenue with the argument that since there was a clear intention on the part of the assessee to give delivery of the commodity and, on the part of the purchaser to take delivery, the receipt could not be treated as damages for breach of contract and not as speculative profit. The Tribunal quoted the language of Explanation 2 and observed :

"The transaction in question having been settled otherwise than by the actual delivery of the commodity, it was a transaction of speculative nature. It was then submitted on behalf of the department that it was only a portion of the contract which was settled otherwise than by actual delivery and therefore, the aforesaid explanation of speculative transaction was inapplicable inasmuch as the said explanation talked of a contract as a whole. We are unable to agree with this contention because under the said explanation a contract may consist of several transactions and if all or any one of them is settled otherwise than by actual delivery of the commodity, to that extent it was a speculative transaction."

In the view taken, the Tribunal held that the sum of Rs. 22,627 was a speculative receipt to the assessee and could not be assessed as business receipt. The Tribunal directed that the profit should now be set off against speculative losses, if any.

Mr. Sabyasachi Mukherji, learned counsel for the revenue, made a two fold submission before us. He analysed the language of Explanation 2 to section 24(1) and submitted that, in the facts of the instant case, the entire contract for supply of 52,000 long tons of Indian iron ore was not settled; part of it was performed and part of the third delivery only remained performed. A settlement, he submitted, which related to a part of the contract would not fit in with the Explanation 2 to section 24(1). He further submitted that what was settled was not a contract, but a claim for damages, based on breach of contract, and that such a settlement would not fall within the language of the Explanation.

We have no decision explaining the Explanation from the point of view we have now to consider. Our attention was invited to a judgment of this court in *D. M. Wadhwa v. Commissioner of Income Tax*, in which G. K. Mitter J. had to consider the language of Explanation 2 to section 24(1) in different context. The facts in that case were that under certain contracts the assessee had to sell to and purchase from the same party the same quantity of the specified commodity of which delivery had to be effected by both on the same day. The parties to a contract exchanged pucca delivery orders which authorised the assessee and the other party respectively to take delivery of the stipulated number of bales from the mills concerned and to draw bills on each other pursuant to the contracts. Debit and credit entries for the entire amount in respect of the pucca delivery

orders were found in the account books and the bank pass books of the assessee. The question was, whether the net loss incurred by the assessee in these transactions could be set off against the other business income of the assessee u/s 24(1) of the Income Tax Act, 1922. In that context his Lordship expressed the opinion that as exchanged of pucca delivery orders amounted only to notional and not real delivery of the goods as contemplated by Explanation 2 to section 24(1), the transactions were speculative transactions and the loss incurred by the assessee could not be set off against the other business income u/s 24(1). His Lordship observed :

"The Explanation to section 24(1), however, does not prevent persons from entering into contracts in which the buyers and sellers may not actually hand over the goods physically. The Explanation is only designed at segregating for Income Tax purposes loss sustained in transactions of a certain kind. It may be that the said transactions are not speculative in the light of section 30 of the Contract Act. It is well-settled that to make a contract wagering within the meaning of section 30 of the Contract Act, there must be a common intention of both the parties to the contract not to give or take delivery but only to deal in differences. The Explanation to section 24(1) goes a step further and takes the transaction out of the domain of intention altogether; only there must be actual delivery or transfer of commodity. The word actual means real as opposed to theoretical or probable..... In enacting the Explanation 2 of section 24(1) of the Income Tax Act, the legislature did not intend to affect any transaction of sale wherein the goods were not physically delivered by the seller to the buyer but only laid down that if there was no actual or physical delivery, the loss, if any, would be a loss in a speculative transaction which could be allowed to be set off only against a profit in a transaction of the same nature."

The above observation, explaining Explanation 2 to some extent, does not cover the problem with which we are confronted in this reference.

Our attention was also invited to another decision of this court in Income Tax Reference No. 87 of 1962 (Commissioner of Income Tax v. Ram Chandra Gupta) in which A. N. Ray J. (D. Basu J. agreeing with him) was pleased to observe :

"The settlement of a contract within the meaning of Explanation 2 to section 24(1) of the Indian Income Tax Act is that the two parties to a contract would settle their respective purchases and sales otherwise than by actual delivery or transfer of the commodity. That is the statutory meaning of settlement."

We are unable to find which statutory meaning was being referred to by his Lordship in the quotation above. Be that as it may, the above judgment also does not in any way help us in resolving the question which we have to decide in this reference.

The two cases being out of the way, we have to interpret section 24(1) with the Explanation and come to our own conclusion. The material portion of section 24(1) is set out below :

"24. (1) Where any assessee sustains a loss of profits or gains in any year or 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, profit 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 actual delivery or transfer of the commodity or scrips :...."

Now a contract may be performed in terms agreed upon. A promise may also be dispensed with or remitted, within the meaning of section 63 of the Indian Contract Act, which reads as follows :

"Every promise may dispense with or remit, wholly or in part, the performance of the promise made to him, or may extend the time for such performance, or may accept instead of it any satisfaction which he thinks fit."

If a contract be neither performed nor dispensed with nor remitted nor otherwise satisfied, there happens a breach of the contract, the consequences of which are to be found in section 73 of the Contract Act, which reads as follows :

"When a contract has been broken, the party who suffers by such breach is entitled to receive, from the party who has broke the contract, compensation for any loss or damage caused to him thereby, which naturally arose in the usual course of things from such breach, or which the parties knew, when they made the contract, to be likely to result from the breach of it.

Such compensation is not to be given for any remote and indirect loss or damage sustained by reason of the breach."

We need not concern ourselves with other consequences of breach, namely, where a party, instead of seeking damages, elects specifically to enforce the broken contract or to obtain an injunction against the party in breach. The same consequence as in section 73 of the Contract Act follows u/s 56 and 57 of the Indian Sale of Goods Act, which are concerned in the following language :

"56. Where the buyer wrongfully neglects or refuses to accept and pay for the goods, the seller may sue him for damages for non-acceptance.

57. Where the seller wrongfully neglects or refuses to deliver the goods to the buyer, the buyer may sue the seller for damages for non-delivery."

We need not concern ourselves with the other remedies for breach of contract

under the Sale of Goods Act, namely, by specific performance or otherwise. In the instant case, part of the contract was not performed. The contract was also not dispensed with or remitted within the meaning of section 63 of the Indian Contract Act. From the facts hereinbefore mentioned, it appears that the assessee proceeded on the footing of a breach of contract by the purchasing Japanese company, namely, its defeat in opening a letter of credit and on that footing claimed damages measured on the difference of price on the date of the breach. As we read Explanation 2 to section 24(1), we do not feel that a claim based on breach of contract comes within the meaning of contract settled as used in Explanation 2. In our reading the expression "contract settled before breach" After breach of contract, the cause of action is no longer based on the contract it self but on its breach. Since the money which the assessee received in the instant case, in our reading of the facts, was the amount of damages suffered by it by reason of breach of the contract, the nature of the transaction was not speculative transaction as defined in Explanation 2. The nature of the contract, which we have recited hereinbefore, give no implication that the contract was of speculative nature. If that contract had been settled we do not know whether it would have fallen within the meaning of Explanation 2. We have held that the contract was not settled but damages for breach of the contract were realised. That makes all the difference and the transaction cannot be characterised as speculative transaction within the meaning of Explanation 2.

The stand taken by the revenue up to the Appellate Assistant Commissioner, was that the claim for damages measured by difference in price was settled. To that aspect of the matter the Tribunal did not advert. The Tribunal proceeded to examine the matter from the point whether only a portion of the contract was settled, otherwise than by actual delivery, and whether that made Explanation 2 inapplicable to the transaction in question. Since the Tribunal was unable to uphold that point, the Tribunal approved of the contention of the assessee and negatived the contention on behalf of the revenue. We are, however, of opinion that the stand taken by the revenue up to the Appellate Assistant Commissioner was a correct stand, in the facts and circumstances of the case, and from that angle of vision the transaction did not fall within the meaning of speculative transaction as in Explanation 2. Since we are of the opinion that the second branch of the submission of Mr. Mukharji ought to succeed, it is not necessary for us to express any opinion on his first contention that settlement of a part of a contract would not fall within Explanation 2 to section 24(1).

In the view that we take, we answer the question referred to us in the negative and against the assessee.

The Commissioner of Income Tax is entitled to costs.

K. L. ROY J. - I agree.

Question answered in the negative.