ITEM NO.63 COURT NO.1 SECTION IIIA

S U P R E M E C O U R T O F I N D I A
RECORD OF PROCEEDINGS

Petition(s) for Special Leave to Appeal (C) No(s). 26114/2008

(Arising out of impugned final judgment and order dated 13/11/2007 in ITA No. 3215/2005 passed by the High Court Of Karnataka At Bangalore)

COMMR.OF INCOME TAX & ANR. Petitioner(s)

VERSUS

M/S KHODAY BREWERIES LIMITED Respondent(s)

(with appln. (s) for c/delay in filing SLP and interim relief and office report)

Date : 29/10/2014 This petition was called on for hearing today.

CORAM :
HON'BLE THE CHIEF JUSTICE
HON'BLE MRS. JUSTICE RANJANA PRAKASH DESAI
HON'BLE MR. JUSTICE A.K. SIKRI

For Petitioner(s) Mr. Mukul Rohatgi, Sr.Adv.
Ms. Rashmi Malhotra, Adv.
Ms. Anil Katiyar, Adv.
Mr. B. V. Balaram Das,Adv.

For Respondent(s) Mr. Mohit Chaudhary, Adv.
Ms. Puja Sharma,Adv.

UPON hearing the counsel the Court made the following
O R D E R

Delay condoned.

Both sides agree that the questions of law raised in this special leave petition are identical with the questions of law raised and considered by this Court in the case of *"Commissioner of Income Tax (Central)-I, New Delhi vs. Vatika Township Private Limited"* 2014 (10)

Scale 510. In the said decision the Court has observed as under :

"38. When we examine the insertion of proviso in Section 113 of the Act, keeping in view the aforesaid principles, our irresistible conclusion is that the intention of the legislature was to make it prospective in nature. This proviso cannot be treated as declaratory/statutory or curative in nature. There are various reasons for coming to this conclusion which we enumerate hereinbelow:

Reasons in Support

39. (a) The first and foremost poser is as to whether it was possible to make the block assessment with the addition of levy of surcharge, in the absence of proviso to Section 113? In *Suresh N. Gupta* itself, it was acknowledged and admitted that the position prior to the amendment of Section 113 of the Act whereby the proviso was added, whether surcharge was payable in respect of block assessment or not, was totally ambiguous and unclear. The Court pointed out that some assessing officers had taken the view that no surcharge is leviable. Others were at a loss to apply a particular rate of surcharge as they were not clear as to which Finance Act, prescribing such rates, was applicable. It is a matter of common knowledge and is also pointed out that the surcharge varies from year to year. However, the assessing officers were in-determinative about the date with reference to which rates provided for in the Finance Act were to be made applicable. They had four dates before them viz.:

(i) Whether surcharge was leviable with reference to the rates provided for in the Finance Act of the year in which the search was inititated; or

(ii) the year in which the search was concluded; or

(iii) the year in which the block assessment proceedings under Section 158 BC of the Act were

initiated; or

(iv) the year in which block assessment order was passed.

The position which prevailed before amending Section 113 of the Act was that some Assessing Officers were not levying any surcharge and others who had a view that surcharge is payable were adopting different dates for the application of a particular Finance Act, which resulted in different rates of surcharge in the assessment orders. In the absence of a specified date, it was not possible to levy surcharge and there could not have been an assessment without a particular rate of surcharge. As stated above, in *Suresh N. Gupta* itself, the Court has pointed out four different dates which were bothering the assessees as well as the Department. The choice of a particular date would have material bearing on the payment of surcharge. Not only the surcharge is different for different years, it varies according to the category of assessees and for some years, there is no surcharge at all. This can be seen from the following table prescribing surcharge for different assessment years:

		PART – I				
Finance Act	Relevant Section of Finance Act	Para - A	Para – B	Para – C	Para – D	Para - E
		IND, HUF, BOI, AOP	Co-operative Society	Firm	Local Authority	Companies
1995	Section 2 (3)	-	-	-	-	
1996	Section 2 (3)	-	-	-	-	15%
1997	Section 2 (3)	-	-	-	-	7.50%
1998	Section 2 (3)	-	-	-	-	-
1999	Section 2 (3)	-	-	-	-	-
2000	Section 2 (3)	10%	10%	10%	10%	10%
2001	Section 2 (3)	12% or 17%	12%	12%	12%	13%
2002	Section 2 (3)	2%	2%	2%	2%	2%
2003	Section 2 (3)	5%	5%	5%	5%	5%

Rate at which tax, or for that matter surcharge is to be levied is an essential component of the tax regime in *Govindasaran Gangasaran* v. *Commissioner of Income Tax*[1], this Court, while explaining the conceptual meaning of a tax, delineated four components therein, as is clear from the following passage from the said judgment :

> **"The components which enter into the concept of a tax are well known. The first is the character of the imposition known by its nature which prescribes the taxable event attracting the levy, the second is a clear indication of the person on whom the levy is imposed and who is obliged to pay the tax, the third is the rate at which the tax is imposed, and the fourth is the measure or value to which the rate will be applied for computing the tax liability. If those components are not clearly and definitely ascertainable, it is difficult to say that the levy exists in point of law. Any uncertainty or vagueness in the legislative scheme defining any of those components of the levy will be fatal to its validity."**

It is clear from the above that the rate at which the tax is to be imposed is an essential component of tax and where the rate is not stipulated or it cannot be applied with precision, it would be difficult to tax a person. This very conceptualisation of tax was rephrased in *C.I.T., Bangalore* v. *B.C. Srinivasa Shetty*[2], in the following manner:

> **"The character of computation of provisions in each case bears a relationship to the nature of the charge. Thus, the charging section and the computation provisions together constitute an integrated code. When there is a case to which the computation provisions cannot apply at all, it is evident that such a case was not intended to fall within the charging section."**

In absence of certainty about the rate because of uncertainty about the date with reference to which

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1 155 ITR 144
2 125 ITR 294

the rate is to be applied, it cannot be said that surcharge as per the existing provision was leviable on block assessment *qua* undisclosed income. Therefore, it cannot be said that the proviso added to Section 113 defining the said date was only clarificatory in nature. From the aforesaid table showing the different rates of surcharge in different years, it would be clear that choice of date has to be formed as in some of the years, there would not be any surcharge at all.

(b) Pertinently, the Department itself acknowledged and admitted this fact which is clear from the manner the issue was debated in a Conference of Chief Commissioners which was held sometime in the year 2001. In this Conference, some proposals relating to simplification and rationalisation of procedures and provisions were noted in respect of block assessment. The foofaraw made in the Conference by those who had to apply the provision, was not without substance because of the garboil situation which this provision had created and in amply reflected in the proposals which was submitted in the following terms:

> **"In the case of a block assessment, there are two problems in relation to the levy of surcharge. The first is that Section 113 does not mention a Central Act. In the absence of a reference to another Central Act in the charging section, it becomes difficult to justify levy of surcharge. Even if it is assumed that reference in the Finance Act to section 113 is a sufficient authority to levy surcharge, the second problem is that the Finance Act levies surcharge on the amount of income-tax on the income of a particular assessment year whereas in the block assessment tax is levied on the undisclosed income of the block period. Absence of a specific assessment year in the block assessment may render the levy suspect. Yet another problem is the rate of surcharge applicable. To illustrate, if the search took place on, say, April 4, 1996, whether the rate of surcharge is to be adopted as applicable to the assessment year 1996-97 or the assessment year 1997-98, the rate of surcharge being different for the two years? The provisions of section 113 or the provisions of the Finance Act do not offer**

any guidance on the issue.

Suggestions :

The foregoing problem indicates that levy of surcharge on undisclosed income is a matter of uncertainty and is prone to litigation. In the circumstances, it is suggested that section 113 may be amended retrospectively in order to provide for levy of surcharge at the rate applicable to the assessment year relevant to the financial year in which the search was concluded."

The Chief Commissioners accepted the position, in no uncertain terms, that as per the language of Section 113, as it existed, it was difficult to justify levy of surcharge. It was also acknowledged that even if Section 113 empowered to levy surcharge, since block assessment tax is levied on the undisclosed income of the block period, absence of specific assessment year in the block assessment would render the levy suspect.

(c) We would like to embark on a discussion on some basic and fundamental concepts, which would shed further light on the subject matter. No doubt, there is no scope for accepting the Libertarian theory which postulates among others, no taxation by the State as it amounts to violation of individual liberty and advocates minimal interference by the State. The Libertarianism propounded by the Australian-born economist philosopher Friedrich A. Hayek and American economist Milton Friedman stands emphatically rejected by all civilised and democratically governed States, in favour of strongly conceptualised "welfare state". To attain welfare state is our constitutional goal as well, enshrined as one of its basic feature, which runs through our Constitution. It is for this reason, specific provisions are made in the Constitution, empowering the legislature to make laws for levy of taxes, including the income-tax. The rationale behind collection of taxes is that revenue generated therefrom shall be spent by the governments on various developmental and welfare schemes, among others.

At the same time, it is also mandated that there cannot be imposition of any tax without the authority of law. Such a law has to be

unambiguous and should prescribe the liability to pay taxes in clear terms. If the concerned provision of the taxing statute is ambiguous and vague and is susceptible to two interpretations, the interpretation which favours the subjects, as against there the revenue, has to be preferred. This is a well established principle of statutory interpretation, to help finding out as to whether particular category of assessee are to pay a particular tax or not. No doubt, with the application of this principle, Courts make endeavour to find out the intention of the legislature. At the same time, this very principle is based on "fairness" doctrine as it lays down that if it is not very clear from the provisions of the Act as to whether the particular tax is to be levied to a particular class of persons or not, the subject should not be fastened with any liability to pay tax. This principle also acts as a balancing factor between the two jurisprudential theories of justice – Libertarian theory on the one hand and Kantian theory along with Egalitarian theory propounded by John Rawls on the other hand.

Tax laws are clearly in derogation of personal rights and property interests and are, therefore, subject to strict construction, and any ambiguity must be resolved against imposition of the tax. In *Billings v. U.S.*[3], the Supreme Court clearly acknowledged this basic and long-standing rule of statutory construction:

> **"Tax Statutes . . . should be strictly construed, and, if any ambiguity be found to exist, it must be resolved in favor of the citizen. *Eidman v. Martinez*, 184 U.S. 578, 583; *United States v. Wigglesworth*, 2 Story, 369, 374; *Mutual Benefit Life Ins. Co. v. Herold,* 198 F. 199, 201, aff'd 201 F. 918; *Parkview Bldg. Assn. v. Herold*, 203 F. 876, 880; *Mutual Trust Co. v. Miller*, 177 N.Y. 51, 57."**

Again, in *United States* v. *Merriam*[4], the Supreme Court clearly stated at pp. 187-88:

> > **"On behalf of the Government it is urged that taxation is a practical**

[3] 232 U.S. 261, at p.265, 34 S.Ct. 421 (1914)
[4] 263 U.S. 179, 44 S.Ct. 69 (1923)

> **matter and concerns itself with the substance of the thing upon which the tax is imposed rather than with legal forms or expressions. But in statutes levying taxes the literal meaning of the words employed is most important, for such statutes are not to be extended by implication beyond the clear import of the language used. If the words are doubtful, the doubt must be resolved against the Government and in favor of the taxpayer. *Gould v. Gould,* 245 U.S. 151, 153"**

As Lord Cairns said many years ago in *Partington* v. *Attorney-General*[5]: "As I understand the principle of all fiscal legislation it is this : If the person sought to be taxed comes within the letter of the law he must be taxed, however great the hardship may appear to the judicial mind to be. On the other hand, if the Crown, seeking to recover the tax, cannot bring the subject within the letter of the law, the subject is free, however apparently within the spirit of the law the case might otherwise appear to be.

(d) There are some other circumstances which reflect the legislative intent. The problem which was highlighted in the Conference of Chief Commissioners on the rate of surcharge applicable is noted above. In view of the aforesaid difficulties pointed out by the Chief Commissioners in their Conference, it becomes clear that as per the provisions then enforced, levy of surcharge in the block assessment on the undisclosed income was a difficult proposition. It is for this reason retrospective amendment to Section 113 was suggested. Notwithstanding the same, the legislature chose not to do so, as is clear from the discussion hereinafter.

"Notes on Clauses" appended to Finance Bill, 2002 while proposing insertion of proviso categorically states that "this amendment will take effect from 1st June, 2002". These become epigraphic words, when seen in contradistinction to other amendments specifically stating those to be clarificatory or retrospectively depicting clear intention of the legislature. It can be seen from the same notes that few other amendments in the Income Tax Act

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5 (1869) LR 4 HL 100

were made by the same Finance Act specifically making those amendments retrospectively. For example, clause 40 seeks to amend S.92F. Clause iii (a) of S.92F is amended "so as to clarify that the activities mentioned in the said clause include the carrying out of any work in pursuance of a contract." This amendment takes effect retrospectively from 01.04.2002. Various other amendments also take place retrospectively. The Notes on Clauses show that the legislature is fully aware of 3 concepts:

(i) prospective amendment with effect from a fixed date;

(ii) retrospective amendment with effect from a fixed anterior date; and

(iii) clarificatory amendments which are retrospective in nature.

Thus, it was a conscious decision of the legislature, even when the legislature knew the implication thereof and took note of the reasons which led to the insertion of the proviso, that the amendment is to operate prospectively. Learned counsel appearing for the assessees sagaciously contrasted the aforesaid stipulation while effecting amendment in Section 113 of the Act, with various other provisions not only in the same Finance Act but Finance Acts pertaining to other years where the legislature specifically provided such amendment to be either retrospective or clarificatory. In so far as amendment to Section 113 is concerned, there is no such language used and on the contrary, specific stipulation is added making the provision effective from 1st June, 2002.

(e) There is yet another very interesting piece of evidence that clarifies the provision beyond any pale of doubt, viz. understanding of CBDT itself regarding this provision. It is contained in CBDT circular No.8 of 2002 dated 27th August, 2002, with the subject "Finance Act, 2002 – Explanatory Notes on provision relating to Direct Taxes". This circular has been issued after the passing of the Finance Act, 2002, by which amendment to Section 113 was made. In this circular, various amendments to the Income Tax Act are discussed amply demonstrating as to which amendments are clarificatory/retrospective in operation and which

amendments are prospective. For example, explanation to Section 158BB is stated to be clarificatory in nature. Likewise, it is mentioned that amendments in Section 145 whereby provisions of that section are made applicable to block assessments is made clarificatory and would take effect retrospectively from 1st day of July, 1995. When it comes to amendment to Section 113 of the Act, this very circular provides that the said amendment along with amendments in Section 158BE, would be prospective i.e. it will take effect from 1st June, 2002.

(f) Finance Act, 2003, again makes the position clear that surcharge in respect of block assessment of undisclosed income was made prospective. Such a stipulation is contained in second proviso to sub-section (3) of Section 2 of Finance Act, 2003. This proviso reads as under:

> **"Provided further that the amount of income-tax computed in accordance with the provisions of section 113 shall be increased by a surcharge for purposes of the Union as provided in Paragraph A, B, C, D or E, as the case may be, of Part III of the First Schedule of the Finance Act of the year in which the search is initiated under section 132 or requisition is made under section 132A of the income-tax Act."**

Addition of this proviso in the Finance Act, 2003 further makes it clear that such a provision was necessary to provide for surcharge in the cases of block assessments and thereby making it prospective in nature. The charge in respect of the surcharge, having been created for the first time by the insertion of the proviso to Section 113, is clearly a substantive provision and hence is to be construed prospective in operation. The amendment neither purports to be merely clarificatory nor is there any material to suggest that it was intended by Parliament. Furthermore, an amendment made to a taxing statute can be said to be intended to remove 'hardships' only of the assessee, not of the Department. On the contrary, imposing a retrospective levy on the assessee would have caused undue hardship and for that reason Parliament specifically chose to make the

proviso effective from 1.6.2002.

40. The aforesaid discursive of ours also makes it obvious that the conclusion of the Division Bench in *Suresh N. Gupta* treating the proviso as clarificatory and giving it retrospective effect is not a correct conclusion. Said judgment is accordingly overruled.

41. As a result of the aforesaid discussion, the appeals filed by the Income Tax Department are hereby dismissed. Appeals of the assessees are allowed deleting the surcharge levied by the assessing officer for this block assessment pertaining to the period prior to 1st June, 2002."

Following the aforesaid decision, this special leave petition is also disposed of in the same terms.

(Neetu Khajuria)
Sr.P.A.

(Vinod Kulvi)
Assistant Registrar