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Court : Mumbai

Decided On : Apr-08-1941

Reported in : [1941]9ITR484(Bom)

Appeal No. : Income-tax Reference No. 1 of 1941

Appellant : All India Spinners Association, in Re.

Judgement :

BEAUMONT, C.J. - This is a reference made by the Commissioner of Income-tax raising a question which he was directed to raise by this Court under Section 66(3) of the Income-tax Act. The question is : 'Whether having regard to the objects of the Association and the manner in which they are carried out and the purpose for which its fund are applied the income of the association is a liable to income-tax and/or super-tax.'

The Association in question is the All India Spinners Association. It was forded as an unregistered Association in the year 1925, and in the year 1937 it was registered under Act XXI of 1860. In the month of March 1938 notice was also served on the assessees under Section 34 of the Act claiming that income had escaped assessment for the accounting year ending December 31, 1935, and at the same time notice was also served on the assessees under Section 22 claiming a return in respect of the accounting year ending December 31, 1936. So that the income with which we have to deal is income which was earned in years when the Association was an unregistered Association. It is claimed that the Association is not assessable to income-tax in respect of profits admitted to have been earned in the accounting years by reason of the exemption contained in Section 4(3)(i) of the Act 1922. That sub-section provides : 'This Act shall not apply to the following classes of income :- (i) Any income derived from property held under trust or other legal obligation wholly for religious or charitable purposes, and in the case of property so held in part only for such purposes, the income applied, or finally set apart for application, thereto.' Then there is a proviso at the end of the sub-section which reads : 'In this sub-section charitable purpose includes relief of the poor, education, medical relief and the advancement of any other object of general public utility.' So that what the assessees have to establish, if they are to avoid liability to tax, is that the income assessed is derived from property held under trust or other legal obligation for religious or charitable purposes.

The Association never possessed any formal trust deed, but there was a document, intended apparently to define its objects which is Exhibit G. It provides in clause 1 : 'Whereas the time has arrived for the establishment of an expert organisation for the development of hand-spinning and khaddar and whereas experience has shown that such development is not possible without a permanent organisation, unaffected and uncontrolled by politics, political changes or political bodies, an organisation called the All India Spinners Association is hereby established with the consent of the All India Congress Committee as an integral part of the Congress organisation, but with independent existence and powers.' In point of fact, the Association could not have any independent existence; it was not registered, and therefore, consisted only of the persons who had become members of the Association. Clause 2 contains the names of the members of the Board of Trustees and Executive Council, and, no doubt, those names suggest that the Association was formed in connection with the Congress Party, a political body. Indeed, that is not disputed. Then clause 4 deals with the objects of the Association, and is in these terms : 'The Council shall have the right to raise loans, to collect subscriptions, to hold immovable property, to invest funds under proper security, to give and take mortgage for the furtherance of hand-spinning and khaddar, to give financial assistance to khaddar organisations by way of loans, gifts or bounties, to help or establish schools or institutions where hand-spinning is taught, to help or open khaddar stores, to establish a khaddar service, to act as agency on behalf of the Congress to receive self-spun yarn as subscription to the Congress and to issue certificates and to do all the things that may be considered necessary for the furtherance of its objects, with power to make regulations for the conduct of affairs of the Association or the Council and to make such amendments in the present constitution, as may be considered necessary from time to time.' It is to be noticed that that document is couched, not in the language of obligation, but of permission. Assuming, however, that it does define the objects, there is nothing therein which limits in any way the purposes for which any profits derived by the Association can be applied. The objects specified do not suggest that profits will be made. The only object, which can result in profits seems to be that of opening khaddar stores. It is further to be noticed that under the concluding words the Council can amend the constitution as may be considered necessary from time to time.

The method in which the Association works and the manner in which the Associations profits were earned are set out in clause 4 of the petition, which the assessees presented to the Assistant Commissioner of Income-tax, appealing against the assessment, and I think I cannot do better than read out the passage. It reads :

'The Association carried out the said objects inter alia in the following manner :- Out of the funds in its hands which have mostly been contributed by donations from the public and subscriptions from the members of the Association, the Association buys Charkhas and hand-looms, and supplies them to the inhabitants of village within the limits of the various branches of the Association free of charge and further buys raw cotton and gives the same to the said persons for the purpose of spinning yarn from such cotton. The Association gives a certain wage to the said persons which, in some cases, is the sole source of income to these persons and in others adds to the earnings of the said persons so as to enable them to maintain and support their families. The yarn so spun is taken over by the Association and supplied to the other persons for weaving cloth on hand-looms. The association also buys hand-spun yarn from the said persons who have spun the same out of their own raw cotton paying them for the same on the basis of the cost of the raw cotton and the wages for spinning the same into yarn. The persons to whom all the yarn is handed over for weaving are also paid a certain wage sufficient either in itself or as an addition to the other income of the persons to maintain and support their families. The wages so paid to the spinners and weavers are not based on the current wages prevailing for similar work but are fixed on the basis of giving to the said persons as far as possible an income sufficient to enable them to support their families. The cloth so woven is taken over by the Association and is sold in the khaddar stores established by the Association in various centers by the branches of the Association. The price charged to the public for such cloth is calculated on the basis of the cost price incurred by the Association in the manner hereinbefore stated plus a certain percentage for shop and over-head charges, without any reference to or connection with the demand for the same and the price of similar mill cloth sold in the market. In the ordinary course the monies realised by the Association by such sales are a little more or less than the cost calculated on the aforesaid basis.'

It appears, that for the years with which we are dealing the Association had decided to increase the amount of wages to be paid to spinners and weavers, with the result that the price which they charge for completed hand-spun cloth had to be increased. However, as I understand it, they sold their stocks of cloth at price based on the increased wages to be paid, whereas in fact that cloth had been manufactured when the reduced scale of wages was in force. The result was that the Association made a profit, and the question is whether such profit is derived from property held under trust or other legal obligation for religious or charitable purposes.

Now, it is argued that this scheme is a scheme for poor relief, the idea being to provide work at certain remuneration to poor agriculturists during that season of the year in which they are not engaged in active agricultural employment. The plea involves, no doubt, subsidising what is essentially an uneconomic industry, because it is admitted that the hand- spun cloth is sold at a price which cannot compete economically with cloth manufactured in the mills, but it is said that the object of the scheme, being to relieve poverty amongst agriculturists, is in its essence a charitable object. If we had not decide whether the scheme falls within the words 'object of public utility' it would be pertinent to observe that the plan is open to criticism. Some economists think that any scheme for diverting industry into uneconomic sources is in the long run bad for a country, other economists may take the view that an industry, although producing no profits, may nevertheless be beneficial to the inhabitants of the country by providing work for an essential class. It may be said too that if this scheme succeeds, and if a large amount of hand-spun cloth is sold, the result will be to diminish the sale of cloth manufactured in mills, and, therefore, whilst relieving poverty amongst agriculturists, the scheme may create poverty amongst mill-hands. But those are really economic questions, and if I had to decide them judicially, I should require to be fortified by opinions of experts. However, I am prepared to assume for the purpose of the present case that this is a scheme for the relief of the poor, and, if so, it is a charitable object, whether or not the Court considers the scheme a wise one. The learned Commissioner considers that it is not to be regarded as a charitable object, because in its essence it is intended to advance the purposes of the Congress, which is a political body. But if one assumes that the object of the Association is relief of the poor, it is none the less charitable, because some political body may consider that it affords the best method of relieving the poor, and may, therefore, adopt the scheme.

But assuming that the Association is in fact carrying out a scheme for the relief of the poor, it seems to me that it fails to bring itself within the exemption under Section 4(3)(i). The Association does not show that the property from which these profits were derived, namely, the hand-spun cloth sold in the Associations shops, is property held under trust or other legal obligation for charitable purposes. At the time when these profits were made, there was no legal obligation upon the Association to devote their profits derived from the sale of cloth to any particular purpose, and the fact that they have in practice, as I will assume, devoted their profits to charitable purposes, does not create any legal obligation. Many people devote a part of their income to charitable purposes, but that does not earn them any exemption from income-tax. There must be a binding legal obligation to devote the income to charitable purposes. It seems to me quite impossible to hold that this Association was bound to devote its profits to charitable purposes. The members of the unregistered Association were free to apply their profits to any purposes they chose.

That being so, in my view the Association have not brought themselves within to exemption, and we must, therefore, answer the question raised in the affirmative.

The assessee to pay costs of the Commissioner.

B J WADIS, J. I am of the same opinion. The question raised by the reference involves consideration of a point of law based on Section 4(3)(i) of the Indian Income-tax Act or 1922, read with the proviso at the end of the sub-section. According to that proviso the expression 'charitable purposes' referred to in the section includes relief of the poor, education, medical relief, and the advancement of any other object of general public utility. Reading the relevant parts of the sub-section and the proviso together, so far as they are applicable for the purposes of the present reference, it follows that in order that the income in dispute may be exempt from payment of income-tax, it must be income derived from property held under trust or other legal obligation wholly either for the relief of the poor or for the advancement of any other object of general public utility. There are, therefore, two points which arise for consideration, namely, (1) whether the property held by the All India Spinners Association is held under a trust or other legal obligation, and (2) whether it is so held for the purposes mentioned above. The amount of the assessment is not in dispute.

Taking the second point first, it was argued that the real purposes for which the property was held was to relieve the poor agriculturists living within the limits of the various branches of the Association. The learned Advocate-general, however, pointed out that the main object was the development of hand-spinning and khaddar as stated in the first clause of the constitution of the Association, and he argued that the carrying out of this object involved only incidentally the relief of the poor agriculturists, like any other industrial venture. I am however, prepared to assume on reading the constitution that the real, underlying object of the Association was to benefit the poor agriculturists in the villages, specially at the time of the year when they are nop actively engaged in agricultural operations. Whether the method employed to relieve this poverty is effective or reasonable from the economic point of view is a matter outside the Courts consideration. But if the object of the Association is the relief of poverty, the fact that the Association is 'an integral part of the Congress organisation', as described in its constitution, is not really material. The Income-tax authorities have laid great stress on this point of the connection of the Association with the Congress. They say in one place that 'the main object of the Association in furthering the production of khadi is political'. In another place it is stated that 'the wearing of khadi is the symbol of the Congress Party just as the wearing of black shirts is the symbol of the Fascists in Italy'. In yet another place it is stated that one of the main objects of the Association was 'to effectively boycott Lancashire cloth'. Whether all this is true or not is also not for the Court to consider, If an association is set on foot by a political organisation and is connected with it, but still has for its real object the relief of poverty, its connection with the political organisation does not, in my opinion, make its real object any the less charitable.

The other point for consideration is whether the property from which the Association derived its profits was held by it under a trust or other legal obligation. A trust is an obligation annexed to the ownership of property. There is, however, no trust-deed not any clear declaration of trust in this case. It is true that no formal or particular words are necessary to create a trust or legal obligation; but the language used must make it certain that the author of the trust intended to create a trust or a legal obligation binding or himself or on the person to whom the property was given. The intention to create a trust or other legal obligation must have be indicated with reasonable certainty. Reading all the words of clause 4 of the constitution of the Association which are relied on they do not indicate a trust or other legal obligation with such certainty; and the Court will not raise such trust or obligation where from the words used the intention to create a trust or obligation is not clearly and definitely expressed. One essential of a trust or a legal obligation is that it should be imperative. In my opinion clause 4 is not couched in language which is imperative or which creates a trust or any other legal obligation. I may also point out that the clause begins by saying that the Council of the Association shall have the 'right' to do all that is mentioned in that clause, and at the end it is stated that the Council may also make such amendments in the present constitution as may be considered necessary from time to time. There are no words in the whole clause which have the binding force of a legal obligation, nor are the real elements of a trust present in them. Clause 3 does not carry the case of the Association any further.

Reference was made in the argument to the case decided by the Privy Council, Trustees of Tribune Press v. Commissioner of Income-tax, Punjab (1) (1939) 7 I.T.R. 415. But in that case it was not disputed that the will of the testator created a trust and directed his trustees to maintain the press in question and the newspaper, namely, the Tribune, for the purpose or object mentioned. The only dispute was whether the purpose or object was one of general public utility within the meaning of the section of the Indian Income-tax Act, and their Lordships helm that it was.

It was stated on behalf of the Association that the surplus amount realised by the sale of the cloth woven out of the hand-spun yarn was also utilised in the same manner as the other funds of the Association, namely, inter alia in getting yarn and cloth manufactured, and providing wages for the person engaged in such manufacture. The learned Counsel for the Association contended that the surplus income was in fact wholly applied or set apart for the same charitable purpose. It seems that that has been the practice of the Association, and that it has been followed ever since it was founded. But a practice, however long, cannot create a trust or a legal obligation under which the property must be held, in order that the income derived from it may be exempt from assessment. It may be that the practice has been followed by the Association because they feel they are bound to do so out of motives of patriotism. But that also cannot create a trust or an obligation which is binding in law. The real question for consideration is whether the income assessed by the Income-tax authorities is income derived from property held under a trust or other legal obligation, and the words and acts relied upon do not effectively create such trust or other legal obligation within the meaning of the section.

For those reasons the question raised in the reference must be answered in the affirmative.

Reference answered in the affirmative.