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April 28

UNION OF INDIA AND OTHERS

v.

GWALIOR RAYON SILK MANUFACTURING (WEAVING) CO. LTD. AND ANOTHER

[P. B. GAJENDRAGADKAR, C. J., K. N. WANCHOO, M. HIDAYATULLAH, K. C. DAS GUPTA AND N. RAJAGOPALA AYYANGAR, JJ.]

Income Tax—Exemption from taxation—Agreement with erstwhile Indian State—Indian State becoming a Part B State under the Constitution of India—Binding nature of the agreement—Finance Act, 1950 (25 *of* 1950), *s.* 13—*Part B States (Taxation Concessions) Order,* 1950, *cl.* 16—*Constitution of India, Arts.* 278, 295, 372.

In October 1946, B wrote to the Government of the erstwhile State of Gwalior stating that certain industries would be established in Gwalior if the Government gave certain facilities including exemption from taxation. The matter was eventually put up before the Ruler who on January 18, 1949, made an order sanctioning the proposals made by the minister which included exemption from taxation as desired by B. On April 7, 1947, an agreement was entered into between the Government and B in accordance with the order of the Ruler dated January 18, 1947, under which certain facilities and concessions were granted to B for the establishment of industries in Gwalior, which included exemption from any form of taxation on the income for a period of 12 years from the date of starting of the factories. In pursuance of the agreement the appellant company was started and actual production began sometime in June 1949 so far as the weaving section of manufacturing cloth from artificial silk yarn was concerned, while the staple fibre section of the company started actual working on or about February 18, 1954. In April 1948 the Ruler of Gwalior entered into a covenant with the rulers of certain other States for the formation of a United State called Madhya Bharat, under which the Rulers made over the administration to the Raj Pramukh. Article VI of the Covenant provided, *inter alia*, that the duties and obligations of the Ruler pertaining or incidental to the Government of the covenanting states shall devolve on the United State and shall be discharged by it. On December 13, 1948, the Madhya Bharat Act, No. 1 of 1948, was passed which provided, *inter alia*, that all laws of the covenanting states shall continue to remain in force until repealed or amended. On January 26, 1950, the Constitution of India came into force and the State of Madhya Bharat became a Part B State under the Constitution. On April 1, 1950, the Indian Income-tax Act, 1922, was extended to the Part B State of Madhya Bharat, and from the same date Finance Act, 1950, also became applicable to that State. The effect of s. 13 of the Act of 1950 was to repeal all laws relating to income-tax prevailing in those parts of India to which the Indian Income-tax Act was extended. On February 25, 1950, an agreement was entered into between the President of India and the State of Madhya Bharat, which was to be in force for a period of ten years under which certain recommendations of Indian States Finances Enquiry Committee were accepted. The Government of India also issued the Part

B States (Taxation Concessions) Order, 1950, by cl. 16 of which, certain concessions were given to industrial undertakings which had been granted exemption from income-tax by the Ruler of an Indian State. In December 1950, the company applied under cl. 16 of the Concessions Order for an exemption from payment of income-tax for the full period of twelve years as provided in the agreement dated April 7, 1947, but the Government of India decided to exempt the company from income-tax and super-tax for the assessment years 1950-51 to 1954-55 in respect of the weaving section and rejected the claim for exemption of the staple fibre section which began working in April 1954. On November 23, 1956, the company filed a suit against the Union of India for a declaration that under the agreement dated April 7, 1947, it was entitled to exemption from income-tax and super-tax for a period of 12 years from June 1949 with respect to the weaving section and for a period of 12 years from February 1954 with respect to the staple fibre section of the company. The company also filed a petition under Art. 226 of the Constitution before the High Court of Madhya Pradesh for the same reliefs.

Held: (i) The order of January 18, 1947, was not a law by which the Ruler of Gwalior granted exemption from income-tax to the company to be established. It only amounted to a signification of the Ruler's acceptance of the request for concessions made by B and an order to his officers to proceed further in the matter after the signification of the Ruler's acceptance of the request.

(ii) In finding out whether a particular order of a Ruler continued under Art. 372 of the Constitution of India as law, the jurisprudential distinction between legislative, judicial and executive acts had to be considered; and only those orders of the Ruler which were jurisprudentially legislative acts would continue as laws under Art. 372.

(iii) The fact that the obligation of the Ruler of Gwalior under the agreement of April 7, 1947, devolved on the Government of India eventually by virtue of Art. 295(1)(b), did not take away the power of Parliament to pass a valid law within its competence which did not transgress the constitutional limitations, and which might affect the obligation arising out of the agreement of April 7, 1947, and even completely supersede it.

(iv) After the extension of the Indian Income-tax Act to Part B State of Madhya Bharat and the passing of the Finance Act, 1950, the exemption claimed by the company under the agreement of April 7, 1947, must fall and the company would only be entitled to (i) reduction in rates provided by the Concessions Order and (ii) such exemption or concessions as the Central Government might grant under cl. 16 of the Concessions Order.

(v) Art. 278(1)(a) merely contemplated an agreement between the Centre and Part B States with respect to levy, collection and distribution of public revenues which were leviable by the Government of India and had nothing to do with any contract between a former Indian State and another person with respect to such revenues which might have become the obligation of the Government of India under Art. 295(1)(b).

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(vi) The Agreement of February 25, 1950, with respect to concessions to corporations must be deemed to have been entered under Art. 295(1)(b) and not under Art. 278(1)(a) and, hence, the company could not rely on that agreement and contend that the agreement of April 7, 1947, was binding for at least ten years thereunder.

CIVIL APPELLATE JURISDICTION: Civil Appeals Nos. 934-935 of 1963. Appeals from the judgment and orders dated August 12, 1960, and April 30, 1960, of the Madhya Pradesh High Court in Civil Suit No. 1 of 1958 and Misc. Petition No. 101 of 1958 respectively.

C. K. Daphtary, Attorney-General, R. Ganapathy Iyer and *R. H. Dhebar*, for the appellants (in both the appeals).

M. C. Setalvad, K. A. Chitale, M. K. Nambyar, Rameshwar Nath and *S. N. Andley*, for the respondents (in both the appeals).

April 28, 1964. The judgment of the Court was delivered by

Wanchoo, J.

WANCHOO, J.—These two appeals on certificates granted by the Madhya Pradesh High Court raise common questions of law and will be dealt with together. The respondent the Gwalior Rayon Silk Manufacturing (Weaving) Company Limited (hereinafter referred to as the company) is registered under the Indian Companies Act. It is necessary to set out how the company came to be established in order to understand the case put forward by the company. In October 1946 Messrs. Birla Brothers Limited, Gwalior, wrote to the Government of Gwalior that they intended to establish at some suitable place in Gwalior a kind of industrial centre in which they intended to set up certain industries provided certain facilities were granted to them by the Government of Gwalior. The facilities for which they made the request were (i) free adequate land at a suitable site; (ii) free processing water if obtainable from a river and at a specially concessional rate if obtainable from a dam; and (iii) exemption from any form of taxation on income for a period of fifteen years from the date of the starting of the factories. On this letter being received, the matter was processed in the Secretariat of the former State of Gwalior. The Secretariat noting shows that the decision to establish industries in Gwalior was largely to be influenced by the decision of the Gwalior Government as to the facilities asked for. The Secretariat also noted that no positive scheme regarding the proposed industrial centre had been submitted but that only tentative proposals were made to ascertain if the State was willing to grant the concessions asked for. It was pointed out that the main question that required consideration was with respect to exemption from any form of taxation on income for a period of fifteen years. It was also pointed out that no income-tax was leviable

in that State at that time and that exemption from income-tax for period of fifteen years would lead to the establishment of the industries which thereafter would yield income in the shape of taxes to the State. It was therefore proposed by the Secretariat that the concessions asked for might be granted. Later, however, the period of exemption from taxation on income was reduced from fifteen to twelve years and it was recommended that this might be granted in order to attract the establishment of industries in the State. The matter was eventually put up before the Ruler on January 18, 1947, and he passed the following order:—

> "The Guzarish of the Minister for Industries, Commerce and Communications dated 15-11-1946 is sanctioned. Exemption from any form of taxation on the income for a period of 12 years from the date of starting of the factories is granted. The other two concessions he has asked for should be given and attempt should be made to establish and start these factories as early as possible."

The substance of this order was communicated to Messrs. Birla Brothers Limited and eventually an agreement was entered into on April 7, 1947 between the Government of Gwalior and Messrs. Birla Brothers Limited, which stated that in accordance with the orders of the Ruler dated January 18, 1947, it was hereby agreed to grant and accord the facilities, privileges, concessions and benefits hereinafter mentioned to the said company. These facilities, privileges, concessions and benefits in the agreement were three, namely—

(1) provision for sufficient and adequate land or lands absolutely free of any cost, revenue or cess whatsoever, for the construction and erection of factory etc. for starting the industries mentioned in the agreement;

(2) making of arrangements for the supply of adequate and sufficient quantities of suitable water, whatever available, for the above-mentioned industries on most concessional and suitable terms;

(3) granting of exemption to the above mentioned industries and/or any concern or concerns promoted or started or to be hereinafter promoted or started for the establishment and starting of all or any of the above-mentioned industries from the payment of all taxes and/or duties, in any form or nature whatsoever, on their incomes, profits, gains or business, levied or to be hereinafter levied in the Gwalior State, or any part thereof, for a period of twelve years reckoned from the date on which the factory or factories of the above-mentioned industries has or have started working or starts or start working.

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In consequence of this agreement, the company was started and actual production began sometime in June 1949 so far as the weaving section for manufacturing cloth from artificial silk yarn was concerned. It may be added that the staple fibre section of the company started actual working on or about February 18, 1954. That is how the company came to be established and started working in what was the former Gwalior State in pursuance of the agreement of April 7, 1949.

Before however the company actually started working even the weaving section for manufacturing cloth from artificial silk yarn, certain constitutional changes took place in India to which it is now necessary to refer. On August 15, 1947, India became a Dominion and the process of mergers which eventually resulted in the emergence of the Republic of India and its Constitution on January 26, 1950, began. In that process, the Rulers of Gwalior, Indore and certain other States in what was known as Central India, entered into a covenant for the formation of the United State of Gwalior, Indore and Malwa (also known as Madhya-Bharat) in April 1948. Article VI of that covenant provided that the Ruler of each covenanting State shall, as soon as may be practicable, and in any event not later than the first day of July 1948, make over the administration of his State to the Raj Pramukh, and thereupon (1) all rights, authority and jurisdiction belonging to the Ruler, which appertain or are incidental to the Government of the covenanting State shall vest in the United State; (2) all duties and obligations of the Ruler pertaining or incidental to the Government of the covenanting State shall devolve on the United State and shall be discharged by it; (3) all the assets and liabilities of the covenanting State shall be the assets and liabilities of the United State; and (4) the military forces, if any, of the covenanting State shall be the military forces of the United State. Clause (2) of this Article also provided that where in pursuance of any agreement of merger, the administration of any other State was made over to the Raj Pramukh, the provisions of cl. (1) would apply to such State as they applied in relation to a covenanting State.

On July 19, 1948, the State of Madhya Bharat acceded to the Dominion of India. On November 24, 1949, the Raj Pramukh of Madhya Bharat issued a proclamation accepting the provisions of the Constitution of India to be framed for the State of Madhya Bharat also. On January 26, 1950, the Constitution of India came into force and the United State of Gwalior, Indore, Malwa became the Part B State of Madhya Bharat.

Meanwhile on December 13, 1948, the United State of Gwalior, Indore, Malwa (Madhya-Bharat) Regulation of

Government Act, No. I of 1948 was passed. Section 4 of that Act provided that "when the administration of any covenanting State has been taken over by the Raj Pramukh or when any State has merged in the United State as aforesaid, all laws, Ordinances, Acts, Rules, Regulations etc., having the force of Law in the said State shall continue to remain in force until repealed or amended under the provisions of the next succeeding section, and shall be construed as if references in them to the Ruler or Government of the State were references to the Raj Pramukh or the Government of the United State respectively". The company contended that by virtue of this Act read with Art. VI of the covenant, the liabilities of the covenanting States devolved on the United State of Gwalior, Indore, Malwa (Madhya-Bharat). Further it was contended that under cl. (b) of Art. 295(1), when the Constitution came into force all rights, liabilities and obligations of the Government of any Indian State corresponding to a State specified in Part B of the First Schedule, became the rights, liabilities and obligations of the Government of India, if the purposes for which such rights were acquired or liabilities or obligations were incurred before such commencement would thereafter be purposes of the Government of India relating to any of the matters enumerated in the Union List. This was subject to any agreement entered into in that behalf by the Government of India with the Government of the State concerned. It was therefore contended on behalf of the company that the obligation incurred by the Ruler of Gwalior by virtue of the agreement of April 7, 1947 became the obligation of the Government of India under cl. (b) of Art. 295(1) on January 26, 1950.

On April 1, 1950, the Indian Income-tax Act was extended to the Part B State of Madhya Bharat. From the same date the Finance Act (No. XXV of 1950) also became applicable to the Part B State of Madhya Bharat by which income-tax became chargeable as provided therein on any income accruing or arising in Madhya Bharat, which by then had become part of India. Further s. 13 to the Finance Act, 1950 provided that "if immediately before the 1st day of April, 1950, there is in force in any Part B State other than Jammu and Kashmir or in Manipur, Tripura or Vindhya Pradesh or in the merged territory of Cooch-Behar any law relating to income-tax or super-tax or tax on profits of business, that law shall cease to have effect except for the purposes of the levy, assessment and collection of income-tax and super-tax in respect of any period not included in the previous year for the purposes of assessment under the Indian Income-tax Act, 1922, for the year ending on the 31st day of March, 1951 or for any subsequent year, or, as the case may be, the levy, assessment and collection of the tax on profits of business

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for any chargeable accounting period ending on or before the 31st day of March, 1949". The effect of this provision was to repeal all laws relating to income-tax in its broadest sense prevailing in those parts of India to which the Indian Income-tax Act was extended from April 1, 1950.

In the meantime, however, agreements were entered into by the Government of India with Part B States in accordance with the recommendation of the Indian States Finances Enquiry Committee, 1948-49 (hereinafter referred to as the Enquiry Committee). The agreement with the State of Madhya Bharat provided that the recommendations of the said Committee contained in Part I of its report read with Chapters I, II, III of Part II of its report insofar as they apply to the State of Madhya Bharat together with the recommendations contained in Chapter IX of Part II of its report were accepted by the parties subject to certain modifications and this agreement was in force for a period of ten years. Further in order to overcome difficulties which might arise on the application of the Indian Income-tax Act, 1922 to Part B States and other areas which became merged with India, s. 60-A was introduced in the Income-tax Act in the following terms:—

> "*Power to make exemption etc., in relation to merged territories or to any Part B State or to Chandernagore*—If the Central Government considers it necessary or expedient, so to do for avoiding any hardship or anomaly, or removing any difficulty that may arise as a result of the extension of this Act to the merged territories.....or to any Part B State....., the Central Government may, by general or special order, make an exemption, reduction in rate or other modification in respect of income-tax in favour of any class of income, or in regard to the whole or any part of the income of any person or class of persons."

In pursuance of this power, the Central Government issued the Part B States (Taxation Concessions) Order, 1950 (hereinafter referred to as the Concessions Order), which fixed reduced rates of income-tax and super-tax for Part B States. Clause 16 of that Order is material for our purpose and was in these terms:—

> "*Concession to industrial undertakings*—(1) Where any industrial undertaking situated in any State claims that it has been granted any exemption from or concession in respect of income-tax or super-tax by the Ruler of an Indian State and was enjoying such exemption or concession immediately before the appointed day it shall submit

an application to the Commissioner of Income-tax giving the following particulars:—

1. Name of the industrial undertaking.
2. Status (ie. whether public or private company, firm, individual or Hindu undivided family).
3. Nature of the business.
4. Date of commencement of the business.
5. Nature of the concession granted.
6. Period for which concessions granted.
7. Unexpired period of the concessions after the appointed day.

(2) Every such application shall be accompanied by the orders in original of the Indian State granting the concession together with a certified copy of the order.

(3) The Commissioner shall, after obtaining such other information as he may require, forward the application to the Central Government which, having regard to all the circumstances of the case, may grant such relief, if any, as it thinks appropriate."

In December 1950, the company applied under cl. 16 of the Concessions Orders for concessions regarding income-tax and super-tax. In November 1951, the company was informed that the Government of India had decided to exempt it from income-tax and super-tax for the assessment years 1950-51 to 1954-55 in respect of the weaving section. The company wanted exemption for the full period of twelve years as provided in the agreement of 1947, but was asked to apply later and eventually the Central Government granted exemption to the weaving section for another five years from 1955-56 to 1959-60. The company's request for exemption of the staple fibre section which began working in April 1954 was rejected by the Government of India.

In the meantime assessment proceedings had been initiated by the Income-tax Officer, A Ward, Gwalior against the company and assessment orders were passed in March 1955, March 1956 and March 1957 with reference to the weaving section for the assessment years 1950-51, 1951-52 and 1952-53. The company appealed to the Assistant Appellate Commissioner against these orders. As the contention of the company was that it was entitled to exemption in accordance with the agreement of April 7, 1947 consequent on the order of the Ruler of Gwalior dated January 18, 1947, it filed a suit on November 23, 1956 against the Union of India for a declaration that under the order dated January 18, 1947 and the agreement

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following thereon, the company was entitled to exemption from income-tax and super-tax and for other reliefs in the alternative. This suit was transferred in 1958 to the High Court on the application of the company under Art. 228 of the Constitution. While this suit was pending, the company filed a petition under Art. 226 of the Constitution on September 11, 1957 in which also it claimed that by virtue of the order of the Ruler of Gwalior dated January 18, 1947 and the agreement following thereon, it was entitled to exemption from income-tax and super-tax for a period of 12 years from June 1949 with respect to the weaving section and for a period of 12 years from February 1954 with respect to the staple fibre section of the company and for other consequential reliefs in the alternative. The High Court of Madhya Pradesh accepted the petition of the company and a direction was issued restraining the Union of India and its officers from making any assessment under the Income-tax Act and levying or collecting income-tax or super-tax in contravention of the exemption given by the agreement dated April 7, 1947. Further the proceedings taken by the income-tax authorities in contravention of the said exemption were quashed. In view of this decision on the writ petition, the High Court decreed the suit in the same terms. The High Court however gave certificates to the Union of India and its officers to appeal to this Court; and that is how there are two appeals before us, one against the decree passed in the suit and the other against order in the writ petition, though as we have said already, the points involved in the two appeals are exactly the same.

Three main contentions were raised on behalf of the company in the High Court. In the first place it was urged that the order dated January 18, 1947 was a special law. It was continued by the State of Madhya Bharat by Act No. 1 of 1948 and it continued after the Constitution came into force by virtue of Art. 372. It was not repealed either by the extension of the Income-tax Act to the State of Madhya Bharat from April 1, 1950 or by s. 13 of the Finance Act, 1950, which applied to the State of Madhya Bharat from the same date. In this connection reliance was placed on the agreement between the President of India and the State of Madhya Bharat dated February 25, 1950 to show that there could be no intention to repeal this special law merely by the extension of the Income-tax Act to the State of Madhya Bharat or by s. 13 of the Finance Act.

In the alternative it was submitted that if the order of January 18, 1947 did not have the force of law the agreement of April 7, 1947 between the Ruler of Gwalior and the company created an obligation which was binding on the former State of Gwalior. That obligation continued to be binding

on the State of Madhya Bharat as it was before the Constitution came into force by virtue of Act No. 1 of 1948 read with Art. VI of the covenant. Further that obligation of the State of Madhya Bharat devolved on the Government of India by cl. (b) of Art. 295 (1) of the Constitution. The obligation thus being a constitutional obligation was not and could not be affected by the extension of the Income-tax Act to the Part B State of Madhya Bharat read with the Finance Act, 1950, and could only be got rid of by an amendment of the Constitution, as cl. (b) of Art. 295 (1) made it into a constitutional obligation which could not be affected even by law.

Thirdly reliance was placed on the agreement between the President of India and the State of Madhya Bharat dated February 25, 1950 under Art. 278 of the Constitution and it was contended that this agreement was binding under Art. 278 (1) (a) of the Constitution and the result of the agreement was that the concessions granted in the agreement in favour of industrial corporations would continue and could not be affected even by the enactment of a law in the shape of the extension of the Income-tax Act to the Part B State of Madhya Bharat read with the Finance Act, 1950.

The High Court held that the order dated January 18, 1947 was a law and that it continued in force by virtue of Act I of 1948 of the State of Madhya Bharat and Art. 372 of the Constitution and that it was not repealed by the extension of the Income-tax Act to the State of Madhya Bharat read with s. 13 of the Finance Act, 1950. It further held that in view of cl. (b) of Art. 295 (1) of the Constitution there was a clear positive instruction in the Constitution that the obligations devolving thereby would be fulfilled and therefore the Government of India was bound to fulfil them irrespective of the extension of the Income-tax Act read with the Finance Act to the State of Madhya Bharat from April 1, 1950. The High Court summed up its conclusion as follows:—

1. that the order dated January 18, 1947 of the Ruler of Gwalior State exempting the company from taxation had the effect of law and the agreement executed on April 7, 1947 cast an obligation on the Gwalior Government to exempt the company from taxation;

2. that by virtue of ss. 3 and 4 of Madhya Bharat Act No. 1 of 1948, the company's right to get the exemption received legislative recognition and the State of Madhya Bharat was bound to discharge the obligation undertaken by the Ruler of the Gwalior State which devolved on it;

3. that it was this obligation of the Madhya Bharat Government to fulfil the obligation undertaken by the Ruler of Gwalior State of granting exemption to the company that

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devolved on the Government of India under Art. 295 (1) (b) and became a constitutional obligation of that Government; and

4. that on a true construction of the relevant provisions of the Income-tax Act, s. 13 of the Finance Act of 1950, and cl. 16 of the Taxation Concessions Order 1950, they did not repeal the specific exemption granted to the company by special statutory provisions and that therefore the company's claim for exemption from taxation was well founded. The argument based on Art. 278 does not seem to have been considered by the High Court; but it has been urged before us by learned counsel for the company in support of the conclusions of the High Court.

The questions that were raised in the High Court have all been raised before us and we now proceed to deal with them *seriatim.*

The first question that falls for consideration is whether the order of January 18, 1947, is a law. In this connection it is contended on behalf of the company that the order must be looked at independently of the agreement of April 7, 1947 which followed it and looked at in that way it must be held to be a law. On the other hand, learned Attorney-General urges that the order was passed by the Ruler in connection with a process which started with the letter of Birla Brothers Limited dated October 17, 1946 and ended with the agreement of April 7, 1947. Birla Brothers Limited had asked for certain concessions in order to enable them to start certain industries in Gwalior and that matter was processed in the Secretariat of the former State of Gwalior. Naturally as concessions could not be granted without the sanction of the Ruler, the matter was put up before the Ruler whether he would agree to grant concessions and the order of January 18, 1947 is nothing more than the Ruler's acceptance of the prayer for grant of concessions which eventually culminated in the agreement of April 7, 1947. The learned Attorney-General therefore contends that the order must be read in the context in which it was passed and if so read, it cannot be law.

Before we consider the rival contentions in this behalf we would like to clear the ground with respect to orders of absolute Rulers. The High Court has relied in this connection on two decisions of this Court, viz., *Ameer-un-Nissa Begum v. Mehboob Begum*(1), and *the Director of Endowments Government of Hyderabad* v. *Akram Ali*(2). In these cases it was observed that the *Firmans* were expressions of the sovereign will of the Nizam and they were binding in the same way as any other law; and therefore so long as a particular *Firman*

(1) A.I.R. 1955 S.C. 352. (2) A.I.R. 1956 S.C. 60.

held the field, that alone would govern or regulate the rights of the parties concerned and that the word of the Nizam was law. It was on these general observations that the High Court relied to hold that the order of January 18, 1947 was law. Since then, however, this Court had occasion to consider these observations in three cases, namely:—(1) *Maharaja Shree Umaid Mills Ltd.* v. *Union of India*(1), (2) *the State of Gujarat* v. *Vara Fiddali Badruddin Mithibar*(2) and (3) *Rajkumar Narsingh Pratap Singh Deo* v. *The State of Orissa*(3). It has been pointed out in these cases that the observations in the earlier cases were not intended to lay down a general proposition that in the case of an absolute monarch no distinction can be made between his legislative and his executive acts. In *Maharaja Shree Umaid Mills Limited*(1), the agreement between the Ruler and the Mills pursuant to the order of the Ruler was held to be a mere contract and not a law within the meaning of Art. 372. The same view has been expressed by four learned Judges in the case of *Vara Fiddali Badruddin Mithibar*(2). Finally in *Rajkumar Narsingh Pratap Singh Deo's case*(3) it was held that this Court had not laid down a general proposition about the irrelevance or inapplicability of the well-recognised distinction between legislative and executive acts in regard to the orders issued by absolute monarchs and that the true legal position was that whenever a dispute arose as to whether an order passed by an absolute monarch represented a legislative act all relevant factors must be considered before the question was answered. These relevant factors were, the nature of the order, the scope and effect of its provisions, its general setting and context, the method adopted by the Ruler in promulgating legislative as distinguished from executive orders, these and other allied matters would have to be examined before the character of the order is judicially determined. We need only add that this must be so when the contention is that a particular order of the Ruler has been continued as a law by Art. 372 of the Constitution. We cannot impute to the Constitution-makers an intention to continue each and every order of an absolute Ruler as a law whatsoever be its nature. When Art. 372 of the Constitution speaks of continuance of laws in 1950 the jurisprudential distinction between legislative, judicial and executive acts must have been present in the mind of the Constitution-makers and that distinction must always be kept in mind by courts in deciding whether a particular order of an absolute Ruler is law for the purpose of its continuance under Art. 372. It may be that the order might not be liable to challenge by any one in the State, while the Ruler was there and in that sense the word of a Ruler might be law in his State. But when we are

(1) [1963] Supp. 2 S.C.R. 515. (2) A.I.R. 1964 S.C. 1043.
(3) A.I.R. 1964 S.C. 1793.

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considering whether a particular order of a Ruler continues under Art. 372 as law we cannot forget the jurisprudential distinction between legislative, judicial and executive acts and only those orders of the Ruler which are jurisprudentially legislative acts will continue as laws under Art. 372 of the Constitution. Therefore simply because the order dated January 18, 1947 was passed by an absolute Ruler it does not necessarily follow that it is law for the purpose of Art. 372 and we have to see after looking into all the various considerations referred to above whether the order can be jurisprudentially said to be a law in order that it may continue as law under Art. 372 of the Constitution.

Let us therefore see the circumstances in which the order came to be passed. We have already referred to the fact that on October 17, 1946, Birla Brothers Limited wrote to the Government of Gwalior saying that they intended to establish in some suitable place in Gwalior a kind of industrial centre in which certain new industries would be located provided certain facilities requested by them were granted by the Government. The facilities requested were three namely, (i) provision for adequate land free at a suitable place (ii) Supply of water free or at a concessional rate, and (iii) exemption from any form of taxation on income for a period of fifteen years from the date of the starting of the factory. It also appears that the industries would have been started in Gwalior only if the concessions were granted. This request in the letter of October 17, 1946 was processed in the Secretariat of the former Gwalior State. The entire file has apparently not been placed before the court but from whatever material is available on the record it appears that there was first a note by the office. Thereafter the Secretary of the department concerned gave his opinion in which it was pointed out that Birla Brothers Limited would only establish industries in Gwalior State if they got the concessions. Then there is the *vinanti* by the Minister concerned. The Minister made it clear that no positive scheme had been submitted but only tentative proposals were made to ascertain if the State would be willing to grant the concessions asked for. The Minister also pointed out that there was no income-tax in the State at that time and so if concession from such taxation was granted it would lead to establishment of industries which after fifteen years might be made liable to such taxes yielding additional income to the State. Therefore the Minister recommended that the concessions as to income-tax as well as the other two concessions might be granted. This report was made on November 15, 1946. On November 17, 1946, the Ruler made the following note thereon:—

"Submit personally on my return". It cannot be the case of the company that even this order of the Ruler requiring papers to be submitted on his return was a law, though

it was certainly an order requiring the Minister to submit papers again when the Ruler returned from somewhere. Then on January 17, 1947, there was a *Guzarish*. In this *Guzarish* it was said that the concessions which had been asked for a period of fifteen years would be accepted if granted for twelve years. It was also made clear that unless such concessions were granted Birla Brothers Limited would not be induced to open factories within the State. Then followed the order of the Ruler dated January 18, 1947, headed Darbar Order, which we have already set out. This order is apparently on the relevant file and it is not in dispute that it was never published, though it was usual by that time in the State of Gwalior to publish laws in some form or other: see, *Madhaorao Phalke* v. *The State of Madhya Bharat*(1).

Apart however from the fact that this order was never published in any form the circumstances in which it came to be made also clearly show that the Ruler while passing the order was merely telling his officers that they could go ahead to comply with the request of Birla Brothers Limited for the three concessions that they wanted. The form of the order also shows that it could not be law. The order consists of three sentences. The first sentence says that "the *Guzarish* of the Minister.....dated 15-11-1946 is sanctioned". Obviously such a sanction for certain concessions cannot be law. Then comes the sentence: "exemption from any form of taxation on the income for a period of 12 years from the date of starting of the factories is granted". It is this sentence which according to the company is law. It may however be mentioned that there was no law as to income-tax in Gwalior State at the time and all that this sentence could mean in the circumstances was that the Ruler was telling his officers that they might assure Birla Brothers Limited that he would not subject them to income-tax for 12 years, even if a law as to income-tax came to be passed later on. In the circumstances we do not think that this sentence which was a promise to exempt Birla Brothers Limited from income-tax, if and when a law of income-tax was passed in future, can jurisprudentially be called a law. Looking at the matter jurisprudentially, the sentence means that if and when the Ruler came to pass a law as to income-tax he would include therein a provision exempting Birla Brothers Limited for the period mentioned in the order. We are therefore of opinion that this sentence even by itself cannot amount to law. Then follows the third sentence, which is divided into two parts. The first part says that "the other two concessions he has asked for should be given". This cannot obviously be law and it is not even contended on behalf of the company that the concessions as to giving of land free and giving of water free or at concessional rate were law. Then follows the second part of the sentence

(1) [1961] I S.C.R. 957, at 966-67.

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which says that "attempt should be made to establish and start these factories as early as possible". This cannot possibly be called law and even the company does not contend that this part of the sentence is a law promulgated by the Ruler of Gwalior. Reading the order as a whole therefore it is obvious that the officers of the Ruler put up the request of Birla Brothers Limited for certain concessions for his order in order that they might be able to go forward and in particular make provision for land and water for the company to be started by Birla Brothers Limited. Therefore as we read this order of January 18, 1947, it appears that by this order the Ruler of Gwalior was saying that he was agreeable to the request of Birla Brothers Limited asking for concessions in order to enable them to start certain industries in Gwalior and that he would grant them concessions if they started industries in Gwalior. This order was apparently communicated to Birla Brothers Limited and it was followed on April 7, 1947 by a formal agreement between the State and Birla Brothers Limited. Whatever doubt might there have been as to the nature of the order, that is in our opinion completely set at rest by the fact that it was followed $2\frac{1}{2}$ months later by an agreement which specifically recited that in accordance with the orders of the Darbar dated January 18, 1947, the agreement was being entered into in order to grant and accord certain facilities etc. to the company. Looking at the matter therefore in the entire context beginning with the letter of Birla Brothers Limited of October 17, 1946 and ending with the agreement of April 7, 1947, all that in our opinion the order of January 18, 1947 says is that the Ruler was agreeable to grant the concessions and that his officers could proceed to take further steps necessary for the purpose. We are not prepared to accept the argument on behalf of the company that the order of January 18, 1947 must be read independently of the agreement of April 7, 1947 simply because the order did not say that an agreement should be taken from Birla Brothers Limited. The absence in the order of any reference to any agreement in our opinion makes no difference in the context in which the order came to be passed and we have no difficulty in holding that the order of January 18, 1947 was not a law by which the Ruler of Gwalior granted exemption from income-tax to the company to be established. It only amounted to a signification of the Ruler's acceptance of the request for concessions made by Birla Brothers Limited and an order to his officers to proceed further in the matter after this signification of the Ruler's acceptance of the request. That the matter was processed further is clear from the fact that on April 7, 1947 an agreement was entered into between the Government of Gwalior and Birla Brothers Limited incorporating the terms acceptance of which had been signified by the Ruler of Gwalior on January 18, 1947. The fact that the

order is called a Darbar Order is again of no significance for it was the Ruler who was signifying his acceptance of the request and the matter was cast in the form of a Darbar Order because his officers would have to carry out what he had decided. There is therefore no doubt that the order of January 18, 1947 cannot be read independently of the agreement of April 7, 1947 and must be read in the context of the entire set of circumstances beginning from the letter of Birla Brothers Limited dated October 17, 1946 and ending with the agreement of April 7, 1947 and so read the order must be held to be a mere signification of the acceptance of the request and cannot be held to be a law even with respect to that part of it which dealt with exemption from income-tax. Further the form and content of the order are against its being a law. Finally the fact that it was never published and remained only on the file concerned has also a bearing on the question and shows that it was not a law but a mere signification of the Ruler's acceptance of the request made by Birla Brothers Limited. It is plain that the order must in the context be treated as one step in the negotiations between the parties which ultimately led to the agreement; and so it would be idle to dissociate it from the said negotiations and treat it as a law. Besides the fact that the parties entered into a formal contract in writing embodying these concessions by the Ruler as consideration for the obligation on the part of Birla Brothers Limited to start the named industries in Gwalior State, is really decisive to negative the argument urged by the company. The agreement having force as a contract—undoubtedly that was the intention both of the Government of the Ruler and Birla Brothers Limited—is wholly irreconcilable with a law operating side by side simultaneously and *de hors* the contract.

As we have come to the conclusion that the order of January 18, 1947 is not a law, we think it unnecessary to consider whether if it was a law it could be said to have been repealed by the extension of the Income-tax Act read with s. 13 of the Finance Act, 1950 to the State of Madhya Bharat. Nor is it necessary to consider what the effect of the agreement between the President of India and the State of Madhya Bharat dated February 25, 1950 would be on the question of repeal and whether that agreement supports the view that in the circumstances there could be no repeal.

This brings us to the alternative argument based on Art. 295 (1) (b) of the Constitution read with the agreement of April 7, 1947. The argument on behalf of the company is that in view of Art. 295(1)(b) the obligation cast on the Ruler of Gwalior by the agreement of April 7, 1947 became the obligation of the Government of India through the Government of Madhya Bharat, and this was a constitutional obligation which could not be affected by the extension of the

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Income-tax Act to the Part B State of Madhya Bharat, from April 1, 1950. It is contended that the obligation being cast by the Constitution its binding force could only be taken away by the amendment of the Constitution and that no law, even if it was good law, could take away the exemption granted by the agreement. On the other hand, learned Attorney-General contends that Art. 295 (1) merely provides in the context of the coming into existence of the sovereign State of the Republic of India for the devolution of the property and assets, and the rights, liabilities and obligations of the Governments of the former Indian States corresponding to State specified in Part B of the First Schedule to the Constitution. He, therefore, contends that Art. 295 (1) (b), when it provides that the liabilities and obligations of any Indian State corresponding to a State specified in Part B of the First Schedule to the Constitution shall in the circumstances mentioned therein be the liabilities and obligations of the Government of India, it only means that for the purposes of the rights and liabilities arising for example out of an agreement between the previous Indian State and any other person, the Government of India will in the circumstances mentioned in Art. 295 (1) (b) be substituted for the Indian State concerned. He further contends that Art. 295 (1) (b) does not in any manner make the liabilities and obligations arising particularly out of contract any the more binding on the Government of India than would have been the case as against the State which originally entered into the contract and that it is not correct to say that Art. 295 (1) (b) cast any constitutional obligation on the Government of India to honour the liabilities and obligations. It is urged that Government of India would have the same defences against a contract as the previous Indian State which originally entered into it would have had, and that Art. 295 (1) (b) is not a fetter on the power of Parliament to legislate in respect of matters with which such contract is concerned and that such legislation would prevail against contract if Paliament was competent to enact it and it did not in any way transgress the constitutional limitations.

We are of opinion that the submission of the learned Attorney-General is correct. Art. 295 appears in Part XII of the Constitution dealing with finance, property, contracts and suits. This Part is divided into three chapters. The first chapter deals with finance and provides for a consolidated fund (Art. 266), a contingency fund if necessary (Art. 267), and for the distribution of public revenues between the Union and the States (Arts. 268 to 272) and grants by the Union to the States (Arts. 273 and 275). Article 277 provides for savings with respect to certain taxes, duties, cesses and fees which were being lawfuly levied by any Government before the Constitution came into force and Art. 278 provides for an

agreement between the Union and the States for a period not exceeding ten years, with respect to certain matters. The other Articles upto Art. 284 in this chapter provide for the Finance Commission and make other miscellaneous provision in financial matters relating to public revenues. These provisions dealing with finances have nothing to do with legislative competence of Parliament or of State legislatures. Articles 285 to 289 certainly affect legislative competence but that is because they make provision in express terms in that behalf. Articles 290 and 291 deal with certain financial adjustments and privy purses of Rulers. Chapter II relates to borrowing and has nothing to do with legislative competence. Then comes Chapter III, which deals with property, contracts, rights, liabilities, obligations and suits. Article 294 provides for the devolution of property and assets, and rights, liabilities and obligations as between the Union and the previous Provinces which became Part A States when the Constitution came into force. Similarly Art. 295 provides for devolution of property and assets, and rights, liabilities and obligations between the Union and what were Part B States when the Constitution came into force. These provisions as to devolution of property and assets, and rights, liabilities and obligations were necessary when the Republic of India came into existence. But there is nothing either in Art. 294 or Art. 295 which in any way fetters the legislative competence either of the Union or of the State legislatures. These provisions had to be made in view of List I and List II which defined the ambit of the power of the Union and the States respectively; but the effect of these provisions so far as rights, liabilities and obligations are concerned, was only to substitute the Union or the States, as the case may be, in place of the old British Indian Provinces or the old Indian States which became respectively Part A and Part B States under the Constitution. These provisions relating to devolution of rights, liabilities and obligations were therefore made only to substitute in place of the old British Indian Provinces and the old Indian States either the Union or Part A or Part B States in accordance with the scheme of division contained in List I and List II of the Seventh Schedule to the Constitution. They did not confer any greater sanctity on contracts, for example, entered into by an old Indian State with other persons, and did not cast any fresh obligation on the Union or the new Part A or Part B State over and above what was already cast on the previous States by contracts when they were made. The defences which would have been open to the old Indian States or the old British Indian Provinces would still be open to the Union or Part A or Part B States against such contracts and the fact that Arts. 294 and 295 provided for devolution made no change in their essential nature as contracts merely. We have not therefore been able to understand what exactly

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is meant by saying that contracts existing from before were converted into constitutional obligations which could only be changed by an amendment of the Constitution and could not be affected even by law validly passed after the Constitution came into force. Stress has particularly been laid on the words "shall be the rights, liabilities and obligations of the Government of India" in Art. 295 (1) (b) and it is suggested that that means that there was clear positive instruction that the obligations so devolving shall be fulfilled. We do not read any such meaning in these words and as we see them they only provide that liabilities and obligations on the Government of India shall be the same as in the case of the previous Indian State which originally entered into contract and therefore the Government of India will have the same defences to such a contract as the previous Indian State would have had; further if the contract could be affected by legislation previously it could equally be affected by legislation after the provision in Art. 295(1)(b). If contracts entered into by the Union could be overborne or nullified by law competently enacted, the obligations devolving on the Union under Art. 295 (1) (b) do not enjoy any higher sanctity or immunity from the effect of legislation. Similar words occur in Art. 294 (b), and what we have said about Art. 295 (1) (b) may be illustrated with respect to Art. 294 (b). Suppose a contract had been entered into by the Dominion of India which was not in accordance with s. 175 of the Government of India Act, 1935, corresponding to Art. 299 of the Constitution. Surely it cannot be contended that simply because Art. 294 (b) says that liabilities and obligations of the Dominion of India shall be the liabilities and obligations of the Government of India, under the Constitution, it would not be open to the Government of India to raise the defence that the contract was not binding on it as it was not entered into in accordance with s. 175 of the Government of India Act, 1935, because these words in Art. 294 (b) amounted to a clear positive instruction that obligations devolving shall be fulfilled. We have no doubt therefore that neither Art. 294 nor Art. 295 cast any such obligation to the effect that the obligation shall be fulfilled, even though it might not have been binding on the previous Indian State which entered into it and even though the previous State might have the right to affect the contract by legislation provided the law passed was valid. The position in our opinion is the same even after the devolution provided in Arts. 294 and 295, and all that these Articles have done is to substitute in place of the previous States or the British Indian Provinces, the Government of India or Part A or Part B States, as the case may be. The devolution of the rights and liabilities prescribed by Art. 295 does not involve and is not intended to involve any change in the character of the said rights and liabilities; and

so pleas which could have been raised in respect of the said rights and liabilities prior to the devolution remain entirely unaffected. There is therefore no question of any constitutional obligation being cast by the provisions contained in Art. 295 (1) (b) on the Government of India to fulfil the contracts irrespective of whether they were binding on the original State which entered into them and whether they can be affected by law validly passed after the Constitution came into force.

We may in this connection refer to the decision in *Maharaja Shree Umaid Mills Ltd.*(1) where it was held that there was nothing in Art. 295 to show that it fettered for all time to come, the power of the Union legislature to make modifications or changes in the rights, liabilities and obligations which had vested in the Government of India. The legislative competence of the Union legislature or even of the State legislature could only be circumscribed by express prohibition contained in the Constitution itself and unless and until there was any provision in the Constitution expressly prohibiting legislation on the subject either absolutely or conditionally, there was no fetter or limitation on the plenary powers which the legislature enjoyed to legislate on the topics enumerated in the relevant lists. There is nothing in Art. 295 which expressly prohibits Parliament from enacting a law as to income-tax in territories which became Part B States and which were formerly Indian States, and such a prohibition cannot be read into Art. 295 by virtue of some contract that might have been made by the then Ruler of an Indian State with any person.

Further in *State of Rajasthan* v. *Shyam Lal*(2), this Court pointed out that even though liability or obligation may be cast on the Government of India or Part A or Part B State by Arts. 294 and 295 of the Constitution, such liability or obligation was always subject to any law made by the new State repealing the old laws and the liabilities arising thereunder or even otherwise, provided the law so made was within the competence of the new State and did not transgress the constitutional limitations.

The fact that the obligation of the Ruler of Gwalior under the agreement of April 7, 1947, devolved on the Government of India eventually by virtue of Art. 295 (1) (b) therefore would not take away the power of parliament to pass a valid law within its competence which does not transgress the constitutional limitations, and which might affect the obligation arising out of the agreement of April 7, 1947, and even completely superseding it.

(1) [1963] Supp. 2 S.C.R. 515. (2) A.I.R. 1964 S.C. 1495.

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We have therefore to see what happened after the Constitution came into force and whether any law was passed by Parliament which in any way affected the agreement of 1947. Reliance in this connection has been placed on behalf of the company on the agreement of February 25, 1950 between the President of India and the State of Madhya Bharat to which we have already referred. That agreement accepted the recommendations of the Enquiry Committee. Our attention is drawn to Part II, Chapter II of the recommendations, where the following recommendation was made in para. 11 (4) (ii):—

> "Any special financial privileges and immunities affecting federal revenues conferred by the State upon other individuals and corporations should ordinarily be continued on the same terms by the Centre, subject to a maximum period of ten (or fifteen) years, and subject also to limiting in other ways any such concessions as may be extravagant or against the public interest."

This recommendation is undoubtedly part of the agreement made between the President of India and the State of Madhya Bharat on February 25, 1950. It is therefore urged that in view of this recommendation in the agreement it was not open to the Government of India to take away the exemption granted by the agreement of April 7, 1947. The agreement between the President of India and the State of Madhya Bharat was entered under Arts. 278, 291, 295 and 306 of the Constitution. It may be accepted that the provision to which we have referred above was entered into by virtue of Art. 295 (1) which provided for devolution of property and assets, and rights, liabilities and obligations subject to any agreement entered into in that behalf by the Government of India with the Government of that State, and to that extent the Government of India was bound to honour the agreement of February 25, 1950. But we have to see what exactly this agreement provides with respect to any special financial privileges and immunities conferred on corporations by the old Indian States. The provision is that privileges and immunities should ordinarily be continued on the same terms by the Centre subject to a maximum period of ten (or fifteen) years. We may emphasise the word "ordinarily" in this provision which shows that the Centre was not bound to continue the privileges and immunities exactly in the same form though "ordinarily" it was expected to do so. Even so, the use of the word "ordinarily" shows that it was open to the Centre to examine the privileges and immunities and decide for itself whether they should be continued and if so in what form and to what extent. Further the provision as to the continuance of the privileges and immunities was subject also to the power of

the Government of India to limiting in other ways any such concession as might appear to it to be extravagant or against the public interest. There was thus a double limitation on the continuance of the privileges and immunities of corporations. Firstly, these privileges and immunities were *ordinarily* to be continued and that in itself imports that in some cases they might not be continued. In the second place the Government of India was given power to limit these privileges and immunities if it was of the opinion that the privileges and immunities were extravagant or against the public interest. This again is a very wide power which the Government of India had even under the agreement of February 25, 1950. Therefore, the argument that the Government of India was bound to continue the privileges and immunities without any modification because of the agreement of February 25, 1960 cannot prevail.

Let us therefore see if any provision was made by the Government of India in this behalf, to carry out this recommendation of the Enquiry Committee. It may be mentioned that the recommendation was made on July 22, 1949 though it was brought into the agreement on February 25, 1950. Section 60-A was introduced in the Income-tax Act by s. 19 of the Taxation laws (Extension to Merged States and Amendment) Act, (No. LXVII of 1949). Originally it only applied to merged territories, but when the Income-tax Act was extended to part B States on April 1, 1950 by the Finance Act, 1950, s. 60-A was amended from the same date and applied to part B States also. Thus it seems to us clear that the provision with respect to immunities and privileges of corporations to which we have already referred was given effect to by the application of s. 60-A which we have already set out above to Part B States. That section provides that if the Central Government considers it necessary or expedient so to do for avoiding any hardship or anomaly or removing any difficulty that may arise as a result of the extension of the Income-tax Act to Part B States, the Central Government may, by general or special order, make an exemption, reduction in rate or other modification in respect of income-tax in favour of any class of income or in regard to the whole or any part of the income of any person or class of persons. Section 60-A therefore clearly provides for the continuance of exemptions where the Central Government thought it necessary so to do. This provision is clearly in accord with the recommendation of the Enquiry Committee to which we have already referred above. This was followed by the Concessions Order, cl. 16 of which specifically referred to concessions to industrial undertakings and provided that the Central Government having regard to all the circumstances of the case might grant such relief if any as it thought appropriate. It may be mentioned further that the same Order

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provided for lower rates of income-tax for some time with respect to all incomes accruing in a Part B State.

The position therefore which emerges on April 1, 1950 is that the income-tax Act was extended to Part B States as from that date by the Finance Act, 1950, and thus income-tax became payable on all income accruing in Part B States subject to the terms of the Finance Act, 1950. Further by the Concessions Order relief was given generally to all income-tax payers in Part B States by reducing the rates of income-tax and there was a special provision in cl. 16 of the Concessions Order with respect to industrial undertakings situated in Part B States which had been granted any exemption from or any concession in respect of income-tax or super-tax by the Ruler of an Indian State and was enjoying such exemption or concession immediately before April 1, 1950. It is not in dispute that it was within the competence of Parliament to extend the Income-tax Act to Part B States and to subject incomes accruing in Part B States to income-tax and super-tax by the Finance Act of 1950. A specific provision was also made in the Income-tax Act by s. 60-A to provide for exemption, reduction in rates or other modifications in respect of income-tax accruing in Part B States, in order to avoid any hardship or anomaly or removing any difficulty which might arise as a result of the extension of the Income-tax Act to Part B States. Lastly by the Concessions Order issued under s. 60-A of the Income-tax Act rates were reduced generally for sometimes and special provision was made with respect to concessions to industrial undertakings in cl. 16. These provisions were all within the competence of parliament and it is not the case of the company that they transgress any constitutional limitation. Therefore as soon as these provisions came into force from April 1, 1950, the result must be that the exemption claimed by the company under the agreement of April 7, 1947 must fall in the face of these legislative provisions and the company would only be entitled to (i) reduction in rates provided by the Concessions Order and (ii) such exemption or concessions as the Central Government might grant under cl. 16 of the Concessions Order. These provisions of law therefore clearly affect the exemption granted by the agreement of April 7, 1947 and after these provisions came into force from April 1, 1950 the company could only get such concessions as were allowable generally under the Concessions Order or specifically under cl. 16 thereof to industrial undertakings covered by that clause. These provisions clearly affect and supersede the agreement and it is not the case of the company that these provisions are not valid. The agreement must therefore be held to have been superseded and the company could only get such benefits as it was entitled to under the Concessions Order. The argument therefore that the obligation arising out of the agreement of 1947 could

not be affected by the extension of the Income-tax Act to Part B State of Madhya Bharat read with Finance Act of 1950 must fail. We have already pointed out what the scope of Art. 295 (1) (b) is and we are of opinion that it was not necessary to amend the Constitution in order to affect the agreement of April 7, 1947. The argument that the Union of India was still bound by the agreement of April 7, 1947 in spite of the legislative provisions made from April 1, 1950 to which we have already referred must therefore fail. The company is therefore not entitled to rely on the agreement of April 7, 1947 for the purpose of exemption and that it can only take advantage of the Concessions Order with respect to income accruing to it in Madhya Bharat. It may be mentioned that the company applied under cl. 16 of the Concessions Order and was given certain exemptions with respect to the weaving section and that is all that the company is entitled to. As to the staple fibre section, the company did apply for exemption under cl. 16, but in all the circumstances the Government of India did not think it fit to grant exemption in that behalf. As that order was in accordance with law the company cannot rest on the agreement of April 7, 1947 which must be deemed to have been superseded by legislative provisions made from April 1, 1950 with respect to income-tax and super-tax in the Part B State of Madhya Bharat. In this connection our attention is drawn to *The South India Corporation Ltd.* v. *The Secretary, Board of Revenue*(1) on behalf of the company. We find nothing in that case which in any way militates against the view that we have taken and it is therefore unnecessary to consider that case in detail. We are therefore of opinion that the High Court was not correct in holding that the Government of India was bound to fulfil the obligation undertaken by the Ruler of Gwalior and was bound to grant exemption to the company under the agreement of April 7, 1947, irrespective of the legislative provisions made with respect to income-tax and super-tax from April 1, 1950.

This brings us to the last contention based on Art. 278 of the Constitution. In this connection the company relies on the agreement of February 25, 1950 to which we have already referred and on the recommendation of the Enquiry Committee, which was made part of the agreement and to which also we have already referred. The argument is that that recommendation must be treated to be an agreement under Art. 278 and would therefore be binding for ten years under that Article and thus the company would be entitled to exemption for at least ten years by virtue of the agreement. We are of opinion that there is no force in this argument. In the first place, the agreement of February 25, 1950 was not merely under Art. 278; it was a composite agreement under Arts. 278, 291, 295

(1) A.I.R. 1964 S.C. 207.

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and 306. We have already pointed out while dealing with the argument based on Art. 295 (1) (b) that this provision of the agreement relating to corporations as to exemptions and concessions to be granted to them may be treated as an agreement under Art. 295 (1), for it dealt with matters of obligation devolving on the Government of India and such devolution was subject to any agreement entered into in that behalf by the Government of India with the Government of the State concerned. But we are unable to see how the provision relating to exemptions or concessions to corporations can be said to be an agreement under Art. 278. The relevant part of Art. 278 (1), on which reliance is placed on behalf of the company is as follows:—

> "(1) Notwithstanding anything in this Constitution, the Government of India may, subject to the provisions of clause (2), enter into an agreement with the Government of a State specified in Part B of the First Schedule with respect to—
>
> (a) the levy and collection of any tax or duty leviable by the Government of India in such State and for the distribution of the proceeds thereof otherwise than in accordance with the provisions of this Chapter;
>
> (b).....
>
> "

Clause (2) of Art. 278 to which cl. (1) is subject merely prescribes the period for which the agreement will remain in force, the maximum being ten years in all. Article 278 appears in Ch. I of Part XII with which we have already dealt with briefly. As we read Art. 278 (1) (a) we find nothing in it which has any relevance with respect to any agreement between Ruler of an Indian State and a corporation. Article 278(1)(a) provides for an agreement between the Government of India and the Government of a Part B State for the levy or collection of any tax or duty leviable by the Government of India in such State and for the distribution of the proceeds thereof otherwise than in accordance with the provisions of Chapter I, Part XII; and this provision is "notwithstanding anything in the Constitution." The earlier provisions in this Chapter provide for the levy and collection of certain taxes and duties leviable by the Government of India and for their distribution between the Government of India and the States. Article 268 (1) deals with such stamp duties and such duties of excise on medicinal and toilet preparations as are mentioned in the Union List and provides that they shall be levied by the Government of India but shall be collected by the States within which such duties are leviable and the proceeds of such duties are to be assigned to that State. Similarly Art. 269 deals with certain other duties and says that they shall be levied and collected by the Government of India but shall

be assigned to the States as provided therein. Article 270 speaks of taxes on income other than agricultural income and lays down that they shall be levied and collected by the Government of India and distributed between the Union and the States in the manner provided thereunder. Article 272 speaks of Union duties of Excise other than such duties of excise on medicinal and toilet preparations as are mentioned in the Union List and lays down that they shall be levied and collected by the Government of India, but, if Parliament by law so provides, there shall be paid out of the Consolidated Fund of India, to the States to which the law imposing the duty extends sums equivalent to the whole or any part of the net proceeds.

It will be clear therefore that the earlier part of the Chapter has provided for levy and collection of certain taxes and duties leviable by the Government of India and the distribution of the proceeds between the Government of India and the States. All that Art. 278 (1) does is to permit by agreement variation in the manner of levy and collection as compared to the provision in the earlier part of the Chapter and also variation in the manner of distribution of the proceeds as compared to the provision in the earlier part. Article 278 (1) (a) only deals with levy and collection of certain public revenues and their distribution between the Government of India and the States. It gives power to the Government of India to enter into agreement with any Government of a State specified in Part B of the First Schedule by which variation may be made in the manner of levy and collection of any tax or duty leviable by the Government of India and the distribution of the proceeds, even though that might not be in accordance with the earlier provisions in the Chapter. Article 278 (1) (a) thus has nothing to do with any obligation arising out of agreements between Rulers of former Indian States and other persons with respect to exemption from any tax or duty. Nor do we see anything in Art. 278 (1) which in any way affects the legislative competence of Parliament or of State Legislatures to pass any law within their respective powers. All that it provides is that the earlier provisions in the Chapter relating to levy, collection and distribution of any tax or duty may be varied for a certain period on an agreement between the Government of India and the Government of a Part B State. This was clearly necessary in view of the fact that many sources of revenue of States which came to form part B States had to be taken over by the Government of India in view of the division of powers of taxation in List I and List II of the Seventh Schedule to the Constitution and that might have created a gap in the revenues of Part B States. Therefore the Government of India was given the power for a period of ten years at the outside to come to an agreement with any Part B State in the matter of levy or collection of any tax or duty leviable by it and its distribution.

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Wanchoo, J.

Article 278(1)(a) would also affect Art. 266 which provides that all revenues received by the Government of India shall form one consolidated fund except the proceeds of certain taxes and duties which were assigned in whole or in part to the States by the other provisions of this Chapter. What Art. 278 (1) does is that it permits the Government of India to enter into agreements not only with respect to levy and collection of duties and taxes specifically dealt with in this Chapter but also with respect to other taxes and duties leviable by the Government of India which would ordinarily go to the Consolidated Fund of India and to provide how such taxes and duties which are made part of the agreement may be levied and collected and in what manner they should be distributed between the Government of India and the Part B State concerned. But for this provision it may not have been open to the Government of India to give help to Part B States which required it beyond what is provided in the earlier provisions of this Chapter. All that Art. 278 (1) does is to provide for further help to Part B States in case it was necessary by entering into agreements with them as to the manner of levy and collection of any tax and duty leviable by the Government of India and for the distribution of its proceeds in spite of the provision in Art 266 requiring all such proceeds to be credited in the Consolidated Fund of India.

When Art. 278 (1) (a) speaks of levy and collection it does not deal with legislative competence but only with the actual levy of tax and its collection; and this in our opinion is clear from the later provision which relates to the distribution of the proceeds resulting from such levy and collection. It is true that sometimes the word "levy" also includes imposition of tax and not merely its assessment and collection; but in the context in which the words "levy and collection" have been used in Art. 278(1), it seems to us that they only cover the assessment and collection not the imposition of a tax. We may in this connection refer to the words of Art. 277 which speaks of any taxes, duties, cesses or fees which were being lawfully levied by the Government of any State or by any municipality or other local authority or body. Those words came up for consideration by this Court in *The Town Municipal Committee* v. *Ramchandra Vasudeo Chimote* (1) and it was held that in the context the words "being lawfully levied" in Art. 277 meant that the tax was actually levied and not merely that a law imposing a tax had been made. Similarly in the context of Art. 278 (1) (a) the levy and collection of any tax, followed as it is by the distribution of its proceeds, mean the actual assessment and collection of the tax and the way in which that should be done and have no reference to legislative competence as to the imposition of the tax. We are of opinion that Art. 278 (1) (a) deals only with public revenues and how they should be assessed and collected

(1) A.I.R. 1964 S.C. 1166.

and distributed between the Union of India and Part B States in case there is an agreement in that behalf between the Union of India and Part B States. It further provides that in case of such agreement the earlier provisions of the Chapter relating to the levy, collection and distribution of taxes and duties would not apply and the agreement would prevail for a maximum period of ten years.

As to the *non obstante* clause with which Art. 278 (1) (a) opens, that was apparently necessary in view of certain provisions of the Constitution as to the extent of the executive power of the Union and the States. Thus it becomes possible to the Government of India if it so decides to enter into an agreement with a Part B State with respect to a tax leviable by the Government of India that the tax shall be assessed and collected by the State through its own officers and the State may retain the entire proceeds so assessed and collected even though the executive power of the Union under Art. 73 extends to matters with respect to which Parliament has power to make laws and ordinarily if a law as to taxation is passed by Parliament within its power its assessment and collection would be by officers under the Government of India. Article 278 (1) (a) however permits that such assessment and collection may also by agreement be left to the States in spite of the provisions in other part of the Constitution. The *nonobstante* clause however with which Art. 278 (1) opens does not in our opinion affect the legislative competence of Parliament even with respect to duties and taxes which are dealt with by an agreement under Art. 278(1)(a). We are therefore of opinion that in the first place the agreement of February 25, 1950 on which the company relies with respect to concessions to corporations must be deemed to have been entered under Art. 295 (1) (b), and not under Art. 278 (1) (a). In the second place, Art. 278 (1) (a) merely contemplates an agreement between the Centre and Part B States with respect to levy collection or distribution of public revenues which are leviable by the Government of India and has nothing to do with any contract between a former Indian State and another person with respect to such revenues which may have become the obligation of the Government of India under Art. 295 (1) (b). The company therefore cannot rely on the agreement of February 25, 1950 in this connection and contend that the agreement of April 7, 1947 was binding for at least ten years thereunder.

We are therefore of opinion that the view taken by the High Court is incorrect. The appeals are therefore allowed and the order of the High Court in the writ petition and the decree of the High Court in the suit are set aside, and the writ petition and the suit are dismissed. In the circumstances we order parties to bear their own costs throughout.

Appeal allowed.