INCOME TAX OFFICER, SHILLONG AND ANR. ETC. A

v.

N. TAKIM ROY RYMBAI ETC. ETC.

February 17, 1976

[R. S. SARKARIA AND S. MURTAZA FAZAL ALI, JJ.] B

Income-tax Act, 1961—*S.* 10(26)(*a*)—*Scope of—Assessee, a person belonging to Scheduled Tribe residing in the specified area—Income accruing or arising in a non-scheduled area—If entitled to exemption.*

Section 10(26)(a), Income-tax Act, 1961 provides that a person is entitled to exemption from income-tax if (1) he is a member of a Scheduled Tribe as defined in Art. 366(25) of the Constitution, (2) he is residing in any area specified in Part A or Part B of the Table appended to paragraph 20 of the Sixth Schedule to the Constitution, or the State or Union Territories mentioned in s. 10(26)(a), and (3) the income in respect of which exemption is claimed is income which accrues or arises to him from any source in the area, State or Union Territories mentioned in the section. C

The assessee belonged to the Jaintia Scheduled Tribe and was a permanent resident of the United Khasi-Jaintia Hills Autonomous District referred to in para 20 of the Sixth Schedule to the Constitution. He was employed in the Secretariat of the Assam Government, and his place of work was within the Shillong Municipality, and was not a part of the area described in para 20 of the Sixth Schedule to the Constitution. The Income-tax Officer held that the income of the assessee from his salary arose in the non-scheduled area and was not covered by the tax exemption provided under s. 10(26)(a). In a writ petition under Art. 226 the assessee challenged the validity of s. 10(26)(a) on the ground that the classification of members of Scheduled Tribes into those having income from a source within the specified areas and those having income from a source outside the areas was arbitrary. The High Court struck it down as violative of Art. 14 on the ground that the exemption clause which was enacted for the benefit of the Scheduled Tribes would be frustrated if the income of such person was made subject to tax merely because the source of that income was outside that area. D E

Allowing the appeals of the Department,

HELD : The High Court was in error in holding that the classification contemplated by s. 10(26)(a), Income Tax Act, 1961, was artificial and was not based on any intelligible differentia. [422D] F

1(a). A taxation law, like any other law, has to pass the equality test of Art. 14, but given the legislative competence, the legislature has ample freedom to select and classify persons, incomes and objects which it would or would not tax. The mere fact that a tax falls more heavily on some in the same category, is not by itself a ground to render the law invalid. It is only when, within the range of its selection, the law operates unequally and cannot be justified on the basis of a valid classification, that there would be a violation of Art. 14. [420B-D] G

East India Tobacco Co. v. *State of Andhra Pradesh,* [1963] 1 S.C.R. 404; *Vivan Joseph Ferriera* v. *Municipal Council of Greater Bombay,* [1972] 1 S.C.C. 70 and *Jaipur Hosiery Mills* v. *State of Rajasthan,* [1970] 2 S.C.C. 27, followed.

(b) Classification for the purpose of taxation or for exempting from tax with reference to the source of the income is integral to the fundamental scheme of the Income Tax Act. The classification made by sub-cl. (a) for the purpose of exemption is not unreal or unknown but conforms to a well recognised pattern and is based on intelligible differentia. The object of this differentiation between income accruing or received from a source in the specified areas and H

A the income accruing or received from a source outside such areas is to benefit not only the members of the Scheduled Tribes residing in the specified areas but also to benefit such areas economically. [420F; 421E-F]

(c) If it is held that a member of the Scheduled Tribe residing in a specified area was entitled to the exemption irrespective of whether the source of his income lay within or outside such area, it may lead to mischievous results. A non-Tribal assessee in India may enter into a sham partnership with a member of the Scheduled Tribe residing in the specified area and ostensibly give him B a substantial share of the profits of the business but really give him only a nominal amount and thus evade tax. Also a tribal residing in the scheduled areas, earning large profits from business located outside the specified areas would be totally exempt while a non-tribal whose source of income is a share in the same business would be taxed and thus the exemption is likely to operate unequally between individuals similarly situated. [421G-H]

(2) The decision in *S. K. Datta, Income Tax Officer and Ors.* v. *Lawrence* C *Singh Ingty*, [1968] 2 S.C.R. 165, on which the High Court had relied is no authority for the proposition that the exemption granted under s. 10(26) to the members of the Scheduled Tribes residing in the specified area, as a class, could not be validly subjected to the condition contained in sub-cl. (a) of that provision. The sentence that "the exemption in question was not given to individuals either on the basis of their social status or economic resources; it was given to a class" occurring in that case could not be torn out of the context and used for spelling out a proposition different from what was actually decided in that case. [419H; F]

D

(3) The State is the best judge to formulate its policies and to decide how far and for what period and in what situations, the members of a particular Scheduled Tribe residing in a particular Tribal area should be afforded the protection and benefit in the matter of promotion of their educational and economic interests embodied in Art. 46 of the Constitution. [422C]

CIVIL APPELLATE JURISDICTION : Civil Appeals Nos. 579 to 594 E of 1975.

Appeals by special leave from the judgment and order dated the 11 October 1974 of the High Court at Gauhati in Civil Rule Nos. 252, 293, 305, 640 and 730 of 1976, and 24, 405, 507 & 510/71, 515 to 517 of 1972 and 165—166 of 1975.

N. M. Lahiri with *D. N. Mukherjee,* for the appellants. (in all the F appeals)

N. M. Lahiri with *D. N. Mukherjee*, for respondents in CAs 579 & 583—586/75.

S. Chaudhuri for respondents in CAs 588 to 590/75

D. N. Mukherjee & R. P. Agarwala, for respondents in CAs 587-590

G

N. M. Lahiri with *D. N. Mukherjee & R. P. Agarwala* for the respondents in CAs 591-592/75

N. M. Lahiri with *D. N. Mukherjee* for respondents in CAs 593-594 of 1975

Ex parte, for respondents in CAs 580-582, 593-594 of 1975.

H The Judgment of the Court was delivered by

SARKARIA, J. These appeals directed against a judgment of the High Court of Judicature at Gauhati raise a common question in regard

to the interpretation and constitutional validity of sub-clause (a) of clause (26) of s. 10 of the Income-tax Act, 1961 (for short, called the 1961 Act). The appeals will be disposed by a common judgment. A

R. Takin Roy Rymbai (respondent in Civil Appeal 579 of 1975) belongs to Jaintia Scheduled Tribe and is a permanent resident of United Khasi-Jaintia Hills Autonomous District under the Sixth Schedule of the Constitution within the State of Meghalaya. He joined service under the Government of Assam in 1941. In the previous year relevant to the assessment year 1970-71, he was posted at Shillong as Secretary to the Government of Assam. The Assam Secretariat building and office, which constitute his place of work was within that quarter of the town which is included in Shillong Municipality and is not a part of the area described in para 20 of the Sixth Schedule. B C

The Income-tax Officer took the view that the assessee's income from salary in the relevant year arose in the non-scheduled area and as such, is not covered by the exemption provided under s. 10(26)(a) of the Act.

The assessee claimed that his income from salary had accrued or arisen within the specified area and, as such, he was entitled to the exemption. In the alternative, he contended that this was not a valid condition for denying him the benefit of the exemption under s. 10 (26). The Income-tax Officer over-ruled these contentions and completed the assessment subjecting the assessee's salary to tax. D

The assessee thereupon filed a petition under Article 226 of the Constitution in the High Court for impugning the assessment orders and the notices of demand for the assessment year 1970-1971, on the ground that sub-clause (a) of s. 10(26) of the Act is invalid and *ultra vires* Article 14 of the Constitution. E

The writ petition was heard by a Bench of three learned Judges of the High Court, which held that this exemption clause has been enacted for the benefit of the Scheduled Tribes residing in specified areas. The object of this exemption clause, according to the High Court, will be frustrated and made nugatory if the income of a member of the Scheduled Tribe residing in the specified areas, is made subject to tax merely because the source of such an income is outside that area. In its view, the classification between members of the Scheduled Tribes having income which accrues or arises to them from any source from the Tribal area or the specified territories on the one hand, and the members of Scheduled Tribe having income which accrues or arises to them from any source outside the Tribal areas or specified territories on the other, is not based on any intelligible differentia; the classification is artificial and is not based on any substantial distinction having a rational nexus to the purpose of the law. On the contrary, the condition contained in sub-clause (a) would defeat the very object of the exemption clause in s. 10 (26). For this enunciation, the High Court has sought support from this Court's observations in *S. K. Dutta, Income-tax Officer and ors.* v. *Lawrence Singh Ingty*(1). F G H

(1) [1968] 2 S.C.R. 165.

A On the above reasoning, the High Court has struck down the aforesaid sub-clause (a) as violative of Article 14 of the Constitution, allowed the writ petition and quashed the impugned notices and the orders of assessment.

The Department has now come in appeal before us after obtaining special leave under Article 136 of the Constitution.

B The provisions of s. 10 of the 1961 Act are in the nature of exemptions. The various clauses of this section indicate the incomes which are to be excluded from computation of the total income of a person under this Act. For a proper perspective, it will be useful to have a look at the historical background of this provision.

C The Indian Income-tax Act, 1922 did not contain any provision specifically exempting members of the Scheduled Tribes from the levy of income-tax. It was the Finance Act 1955 that first incorporated in the Income-tax Act, 1922 provisions for exemption of the Tribal people of the eastern region from payment of the tax. These provisions relating to such exemptions were further amended and recast by s. 3 of the Finance Act 1958 as follows :

D "S. 4(3) XXI. Any income of a member of a Scheduled Tribe defined in clause (25) of Article 366 of the Constitution, residing in any area specified in Part A or Part B of the Table appended to paragraph 20 of the Sixth Schedule to the Constitution or in the Union Territories of Manipur and Tripura, provided that such member is not in service of Government."

E The 1961 Act then re-enacted this clause as under :

"10 (26) In the case of a member of a Scheduled Tribe as defined in clause (25) of Article 366 of the Constitution, residing in any area specified in Part A or Part B of the Table appended to paragraph 20 of the Sixth Schedule to
F the Constitution or in the Union Territories of Manipur and Tripura, who is not in the service of Government.

any income which accrues or arises to him.

(a) from any source in the area or Union Territories aforesaid, or

G (b) by way of dividend or interest on securities."

The State of Nagaland (Adaptation of Laws on Union Subjects) Order 1965 added with effect from the 1st December 1963, the State of Nagaland also, to the areas, the Tribal people of which could claim this exemption.

H The validity of the exclusion of the Government servants from the exemption given under s. 10(26), as it stood before the amendment of 1970, came up for consideration before this Court in *S. K. Datta, Income-tax Officer and ors.* v. *Lawrence Singh Ingty* (supra). It was held that the classification of Tribals into Government servants

and others for purposes of this exemption was violative of Article 14 of the Constitution and, as such, invalid. A

Thereafter, Parliament passed the Taxation Laws (Amendment) Act 42 of 1970 whereby the words "who is not in the service of the Government" appearing in s. 10(26), were deleted. The North Eastern Areas (Reorganization) (Adaptation of Laws on Union Subjects), Order 1974 amended this provision further with effect from January 25, 1972 so that it now reads as follows : B

> "(26) in the case of a member of a Scheduled Tribe as defined in clause (25) of Article 366 of the Constitution, residing in any area supecified in Part A or Part B of the Table appended to paragraph 20 of the Sixth Schedule to the Constitution (or in the State of Nagaland) Manipur and Tripura or in the Union Territories of Arunachal Pradesh and Mizoram or in the areas covered by Notification No. TAD/R/35/50/109, dated the 23rd February 1951, issued by the Governor of Assam under the provisions to sub-paragraph (3) of the said paragraph 20 (as it stood immediately before the commencement of the North Eastern Areas (Reorganization) Act 1971 (81 of 1971) any income which accrues or arises to him, C D
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> (a) from any source in the (area, State or Union territories) aforesaid, or
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> (b) by way of dividend or interest, on securities".

An analysis of this provision shows that in order to entitle a person to the exemption, three conditions must co-exist : E

> (i) He should be a member of a Scheduled Tribe as defined in Clause (25) of Article 366 of the Constitution;
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> (ii) He should be residing in any area specified in Part A or Part B of the Table appended to paragraph 20 of the Sixth Schedule to the Constitution; or the State or Union Territories mentioned in this provision; F
>
> (iii) The income in respect of which exemption is claimed must be an income which accrues or arises to him—
>
> (a) from any source in the area, State or Union territories mentioned in the provision or G
>
> (b) by way of dividend or interest, on securities".

Article 366(25) of the Constitution provides :

> "Scheduled Tribes" means such tribes or tribal communities or parts of or groups within such tribes or tribal communities as are deemed under article 342 to be Scheduled Tribes for the purposes of this Constitution." H

Article 342 empowers the President with respect to any State or Union Territory, and where it is a State, after consultation with the

A Governor thereof, by public notification, to specify Tribes or Tribal communities or parts of or groups within tribes of tribal communities which shall for the purpose of this Constitution be deemed to be Scheduled Tribes, as the case may be. Clause (2) of this Article empowers the Parliament to exercise the some power by enacting a law.

B The respondent belongs to Jaintia Scheduled Tribe which is one of the Scheduled Tribes notified under Art. 342(1). The first condition for applicability of s. 10(26) was thus indubitably satisfied.

Part II of the Table appended to paragraph 20 of the Sixth Schedule of the Constitution *inter alia* specifies the United Khasi-Jaintia Hills District as one of the Tribal Areas. According to the C averments in the writ petition, the respondent is a permanent resident of the United Khasi-Jaintia Hills autonomous District. This allegation has not been denied by the other side. Indeed, in the petition for special leave to appeal filed by the appellant the fact that he is a resident of a Tribal area specified in Paragraph 20 of the Sixth Schedule to the Constitution, is admitted.

The first two conditions necessary for claiming exemption under D s. 10(26) existed in the present case. Whether on the facts of the case, the third condition embodied in sub-clause (a) was satisfied or not, is a question which still remains to be determined. The High Court has advisedly left it open. The controversy has thus narrowed down into the legal issue : whether the classification made by sub-clause (a) for the purpose of the exemption under s. 10(26) between the income of a member of a Scheduled Tribe accruing or E arising from any source in the area, State or Union Territories specified in the aforesaid Clause (26), and the income from a source outside such area, State or Union Territories is constitutionally valid?

In answering this question in the negative, the High Court has propounded the proposition that the object of clause (26) of s. 10 is to grant a blanket exemption to members of Scehduled Tribes *as a* F *class* residing in the specified areas, and that the condition contained in sub-clause (a) is destructive of that object. In propounding this proposition, the learned Judges seem to have relied on certain observations of this Court in *Lawrence Singh Ingty's case* (supra).

Mr. Lahiri appearing for the respondent, also, reiterates the reasoning of the High Court that the exemption was given to the Tribal people as a class, and not on the basis of their economic resour- G ces or sources of income. In this connection Counsel has cited a few sentences from this Court's judgment in *Lawrence Singh Ingty's case* (supra).

With due respect to the learned Judges of the High Court, we are unable to accept this reasoning. The matter now in controversy was not even obliquely in issue before this Court in *Lawrence Singh Ingty's* H case. Therein, the only question for decision was, whether the exclusion of the Government servants from the exemptions given in s. 4(3)(XXI) of the Indian Income-tax Act, 1922 and later on in s. 10 (26) of the Income-tax Act 1961, was violative of Article 14 of the Constitution.

Although sub-clause (a) was very much there, its validity was not, even indirectly questioned. The contention of the Revenue, therein, was that the exemption from income-tax was given to members of certain Scheduled Tribes, due to their economic and social backwardness; that it was not possible to consider Government servants as socially and economically backward and hence the exemption was justly denied to the assessee, who was a Government servant having income from salary. It was further urged by the Revenue that once a Tribal becomes a Government servant, he is lifted out of his social environment and assimmilated into forward sections of society and therefore he needs no more any crutch to lean on.

These arguments were found to be irrelevant and unsustainable. In that context, the Court observed :

> "*The exemption in question was not given to individuals either on the basis of their social status or economic resources. It was given to a class.* Hence individuals as individuals do not come into the picture.
>
> We fail to see in what manner the social status and economic resources of a government servant can be different from that of another holding a similar position in a corporation or that of a successful medical practitioner, lawyer architect, etc. To over-paint the picture of a government servant as the embodiment of all power and prestige would sound ironical. Today his position in the society to put at the highest is no higher than that of others who in other walks of life have the same income. For the purpose of valid classification what is required is not some imaginary difference but a reasonable and substantial distinction having regard to the purpose of the law."

The sentences which have been underlined are the sheet-anchor of the arguments advanced by Mr. Lahiri. In our opinion, they cannot be torn out of the context and used for spelling out a proposition different from what was actually decided in that case. The *ratio* of that decision is that within the members of the Scheduled Tribes residing in specified areas selected by the State for the purpose of exemption, the miniclassification between *individuals* who were government servants deriving income from salary and those who were not such government servants, was not based on intelligible differentia. Since there was no rational basis whatever for this differentiation, it was held that within the range of the selection, the government servants had been unfairly discriminated against lawyers, medical practitioners, private servants, businessmen, etc. whose income was derived from non-government sources, and that the exclusion of government servants from the exemption under s. 10(26) was bad and unconstitutional. This vice of discrimination from which s. 10(26) was then suffering, was removed when the Amending Act 42 of 1970 exercised the obnoxious limb of the provision.

The decision in *Lawrence Singh Ingty* is thus no authority for the proposition that the exemption granted under s. 10 (26) to the members of the Scheduled Tribes residing in the specified areas, as a class,

could not be validly subjected to the condition contained in sub-clause (a) of the provision.

While it is true that a taxation law, cannot claim immunity from the equality clause in Article 14 of the Constitution, and has to pass like any other law, the equality test of that Article, it must be remembered that the State has, in view of the intrinsic complexity of fiscal adjustments of diverse elements, a considerably wide discretion in the matter of classification for taxation purposes. Given legislative competence, the legislature has ample freedom to select and classify persons, districts, goods, properties, incomes and objects which it would tax, and which it would not tax. So long as the classification made within this wide and flexible range by a taxing statute does not transgress the fundamental principles underlying the doctrine of equality, it is not vulnerable on the ground of discrimination merely because it taxes or exempts from tax some incomes or objects and not others. Nor the mere fact that tax falls more heavily on some in the same category, is by itself a ground to render the law invalid. It is only when within the range of its selection, the law operates unequally and cannot be justified on the basis of a valid classification, that there would be a violation of Article 14. (See *East India Tobacco Co.* v. *State of Andhra Pradesh*(1) *Vivian Joseph Ferriera* v. *Municipal Council of Greater Bombay;*(2) *Jaipur Hosiery Mills* v. *State of Rajasthan.*(3)

The validity or otherwise of the classification of income envisaged by sub-clause (a), with reference to the source of income, for the purpose of the exemption under s. 10(26) is to be judged in the light of the above principles.

Classification for purposes of taxation or for exempting from tax with reference to the source of the income is integral to the fundamental scheme of the Income-tax Act. Indeed, the entire warp and woof of the 1961 Act has been woven on this pattern.

Section 2(45) defines total income to mean "the total amount of income referred to in s. 5 computed in the manner laid down in this Act".

Section 5 makes the chargeability of income dependent upon the locality of accrual or receipt of the income. It defines the extent of total income with reference to the residence of the assessee, and thus makes the incidence of taxation dependent upon whether the assessee is a resident in India. It is the residence in India which entails liability to tax. A non-resident is not liable in India to get his income assessed, but if any part of his income accrues or arises whether directly or indirectly through any business connection in India or from any property in India, the same would be assessable. An ordinary resident as defined in s. 6, does not attract additional chargeability but being "not ordinarily resident" entitles a person to partial exemption from

(1) [1963] 1 S.C.R. 404. (2) [1972] 1 S.C.C. 70.

(3) [1970] 2 S.C.C. 27.

chargeability as a resident, to which exemption a person who is "ordinarily resident" is not entitled—(see Kanga and Palkhivala Vol. I—Income-tax 6th Edn. p. 162). A

The 1961 Act abounds in instances whereby certain sources of income have been exempted from tax, while others are assessable.

Section 10 of the 1961 Act, itself contains no less than 30 instances of such classification for the purpose of granting exemptions from tax. This is so, in spite of the fact that another source of the same person's income may be assessable. A person may have agricultural income apart from salary or business income. The income from the former source is not to be included in the total income of the assessee (vide s. 10(1)); while income from the latter source is not so exempted. Again, interest realised from Scheduled banks on deposits upto a certain limit is exempt, while interest realised from non-banking concerns is assessable. B C

Sections 80A to 80U further provide exemptions from tax to incomes derived from certain sources. A business man's income is assessable, but if it is from a newly established industrial undertaking or priority industry, to that extent, the same is exempted. Section 80H provides for deductions in cases of new industrial undertakings employing displaced persons etc. D

It is not necessary to multiply such instances. Suffice it to say that classification of sources of income is integral to the basic scheme of the 1961 Act. It is nobody's case that the entire scheme of the Act is irrational and violative of Article 14 of the Constitution. Such an extravagant contention has not been canvassed before us. Thus the classification made by the aforesaid sub-clause (a) for purposes of exemption is not unreal or unknown. It conforms to a well recognised pattern. It is based on intelligible differentia. The object of this differentiation between income accruing or received from a source in the specified areas and the income accruing or received from a source outside such areas is to benefit not only the *members* of the Scheduled Tribes residing in the specified areas but also to benefit economically such *areas*. If the contention advanced by Mr. Lahiri is accepted and a member of the Scheduled Tribe residing in a specified area is held entitled to the exemption irrespective of whether the source of his income lies within or outside such areas, it will lead to potentially mischievious results and evasion of tax by assessees who do not belong to the Scheduled Tribes. All that a non-tribal assessee in India need do would be to enter into a sham partnership with a member of the Scheduled Tribe residing in the specified area and ostensibly give him under the partnership a substantial share of the profits of the business while, in reality, pay the tribal only a nominal amount. Moreover, but for the condition provided in sub-clause (a), the exemption granted under s. 10(26) is likely to operate unequally and cause inequality of treatment between individuals similarly situated. A Tribal residing in the Scheduled areas earning large income from business located outside the specified areas, would be totally exempt while the non-tribal whose source of income is a share in the same business would be taxed although with reference to the source of the income, both were similarly situated. E F G H

A We are not persuaded to accept Mr. Lahiri's argument that the making of the exemption conditional upon the classification envisaged by sub-clause (a) would deter the members of the Scheduled Tribes from joining the mainstream of national life, or, would be inconsistent with the Directive Principle embodied in Article 46. This Article contains a Directive Principle of State Policy for promotion of educational and economic interests of the weaker sections of the people, particular-
B ly the Scheduled Castes and Scheduled Tribes. Its primary objective is to provide protection to the "weaker sections" of society. Members of the Scheduled Tribes who are enterprising and resourceful enough to move out of the seclusion of the tribal areas and successfully compete with their Indian brethern outside those areas and rise to remunerative positions in service or business, cease to be "weaker sections". In any case, the State is the best judge to formulate its policies and to
C decide how far and for what period and in what situations, the members of a particular Scheduled Tribe residing in a particular Tribal area should be afforded the protection and benefit in the matter of promotion of their educational and economic interests.

In view of what has been said above, we are of opinion that the learned Judges of the High Court were in error in holding that the
D classification contemplated by sub-clause (a) of cl. (26) of s. 10 of the 1961 Act is artificial and is not based on any intelligible differentia. We would therefore, reverse the judgment of the High Court and hold that the aforesaid sub-clause (a) is constitutionally valid.

Before we part with this judgment, we may note that Mr. Lahiri made a detailed survey of the history of the Tribal areas of Assam and
E Scheduled Tribes residing in those 'autonomous' areas. Counsel also argued that virtually the source of the salary received by the assessee lay in the Tribal areas forming the State of Meghalaya, notwithstanding the fact that on account of the exigencies of service, the office of the assessee was located in those Wards of Shillong which are not a part of the tribal areas. In our opinion, it is not necessary to go into this question which, as already noticed, still remains open and undeter-
F mined.

In the result we allow these appeals, but in the circumstances of the case, leave the parties to pay and bear their own costs.

P.B.R. *Appeals allowed.*