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CRITICAL ANALYSIS OF RULES OF INTERPRETATION
APPLICABLE TO TAXING STATUTES

SAHANA S

1. INTRODUCTION

Interpretation of Statute means obtaining the true meaning of the provisions or the intention of the legislature. In other words it is the process by which the courts seek to ascertain the meaning of legislature through the medium of authoritative forms in which it is expressed. There are various rules and principles with respect to the Interpretation of statutes. The four core rules of interpretation are the Mischief rule, Golden rule, Literal rule and rule of Harmonious Construction. The Statutes are broadly classified into various types so as to enable the application of the said rules of interpretation. Application of the rules of interpretation highly depends on the nature of the statute, for example the procedural laws are interpreted liberally in order to enforce the substantive legislations.

Tax is a charge on a person, which is the primary source of revenue for the Sovereign Authority. The Natives or inhabitants of the State must contribute to its revenue by paying taxes proportionate to their abilities, where the said tax is not arbitrary but rather certain, and the modus operandi of collecting tax is convenient for the taxpayers and economical for the State.

One of the classifications or types of statute is Taxing statute. It enables the Sovereign authority to impose tax on the citizens. The Constitution of India authorizes both the Centre and states to enact taxing legislations.

The Government is the only authority that is vested with the power of imposing or collecting tax. In the words of the Constitution, No tax shall be levied or collected except by authority of law.

This paper seeks to analyze the rules of interpretation applied to Taxing statutes.

2. APPLICATION OF RULE OF STRICT CONSTRUCTION TO TAXING STATUTE:

It is well established principle that the taxing statutes are interpreted in strict sense. The Courts often apply rule of strict construction while interpreting the provisions of a taxing

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1Salmond, Jurisprudence, 11th Edition, p 152
2An Inquiry into nature and causes of Wealth of Nations, Adam Smith, P.640
3Constitution of India, Schedule VII
4Constitution of India, Article 265
statute. Reliance is made on the natural and grammatical meaning of the words used in the provision. In strict construction, no equitable or reasonable considerations are given while interpreting an ambiguous provision, but rather the exact or literal meaning of the provision is taken into consideration. There are three stages involved in the process of imposition of tax. Firstly the person (both natural and juristic) liable to pay tax should be identified. Secondly the assessment of tax and thirdly the mode of recovery if the said person fails to comply with his duty to voluntarily pay tax. The first stage implies the charging provisions of the Act and those provisions are interpreted in strict sense.

While interpreting a taxing statute, the words or the text of the provisions of that statute are simply adhered to and there is no scope for assumptions and reasonable construction and if more than one reasonable interpretation of taxing statute is available, the one that favors the assessee has to accepted. This was clearly expressed by Rowlatt J stating “There is no room for intendment and there is no equity about a tax. There is no presumption as to tax and nothing is implied. One can only look fairly at the language used.” Textualist approach is generally adhered to while interpreting fiscal legislations like taxing statutes. According to this approach, the legal effect of the statute must be consistent with the linguistic meaning of its provisions. Unlike purposivism, this approach does not dwell on the objective purpose of the statute.

The rule of strict construction is applied to charging provisions of the Taxing statute because it imposes a financial burden on the taxpayer. These provisions express or outline the subjects covered within the statute, like a natural person being a resident of the country is one of the subjects who fall within the scope of charging provisions of the Taxing statute. The rule of strict construction is applied based on the notion that the legislature is the body that is empowered to rectify the absurdity. The lawmakers described the provisions of the statute in such a way for a reason and the court cannot extend its scope. This notion was well expressed in the case of “State of Uttar Pradesh v. Kores India Pvt ltd”\(^5\), in which the Court observed that the word ‘paper’ does not include ‘carbon paper’ within its meaning for the purpose of sales tax, since the legislature did not expressly make it a subject to tax. Thus the court cannot extend the scope of the meaning of a term in order to include a subject for the purpose of taxation. The Supreme Court even refused to apply the principle of logic and reasoning while interpreting the meaning of the term ‘dependent’ under section 2(g) of

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5\(^{\text{Cape Brandy Syndicate v IRC, (1921) 1 KB 64}}\)
6\(^{\text{AIR 1977 SC 132}}\)
Expenditure Tax Act, 1957.\(^7\) Therefore the rule of strict construction is applied to the charging provisions of the Taxing statutes. The reason for application of strict rule was well expressed in the case of “Pryce v Monmouthshire Canal & Railway Co”\(^8\) in which Lord Cairns observed that since there is neither any priori liability in the subject to pay any particular tax, nor an antecedent relationship between the tax payer and the taxing authority, no reasoning could be established upon any supposed relationship between the tax payer and the taxing authority that could be brought to bear upon the construction of the Act.\(^9\)

3. APPLICATION OF STRICT RULE TO EXEMPTIONS:

Apart from charging provisions, the strict rule is also applied to the exempting provisions. The General rule is strict interpretation of exemptions.\(^10\) The strict rule is applied to the exempting provisions if the ambiguity is with respect to its applicability. It is construed in strict sense while deciding upon whether the subject falls within the exemption clause and once this ambiguity or doubt is lifted, the provision can call for wider and liberal construction. \(^11\)

In the case of “State of Gujarat v Essar Oil Ltd”\(^12\), the rule of strict construction was applied by the court in the construction of an exception. The court also observed that the general principle of construction in favor of the assessee in case of ambiguity is not always applicable to the exempting provisions. However in the case of “Innamuri Gopalam and Maddala Nagendrudu v State of A. P”, the court held in the favour of the assessee. It was contended in this case that the intention of the alleged notification was to avoid double taxation and so the assessee was not granted tax exemption available under the said notification. The court applied strict rule of construction and held that the assessee was entitled to the exemption.

4. APPLICATION OF RULE OF LIBERAL CONSTRUCTION TO TAXING STATUTE:

The machinery provisions (i.e. provisions with respect to assessment and recovery of tax) of the taxing statute are generally liberally construed. Courts, in plethora of cases applied rule of liberal construction with respect to machinery provisions. The plain or literal reading of the

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\(^7\) Azamjha v Expenditure Tax Officer, Hyderabad, AIR 1972 SC 2319  
\(^8\) (1879) 4 AC 197  
\(^9\) Id, p.202  
\(^10\) Commissioner of Customs v M Ambalal & Co, (2011) 2 SCC 74  
\(^11\) UOI v Wood Papers Ltd, AIR 1991 SC 2049  
\(^12\) (2012) 3 SCC 522
§18-A (6) of the Income Tax Act, 1922, makes it inapplicable to the cases under subsection 8 of the same provision. But being a machinery provision it was construed liberally so as to include the cases under subsection 8 within its scope.\textsuperscript{13}

The penalty provisions of the Taxing statute are not equated to penal or criminal statute which impliedly requires the element of mens rea, unless the language of the statute expressly states so. In the case of \textit{“Commissioner of Central Excise & Customs, Mumbai v ITC Ltd”},\textsuperscript{14} it was observed by the court that the penalty provision should be interpreted by applying the golden rule and before the penalty can be levied the procedure laid down in the Act must be complied with.

Therefore, the rule of strict construction is applied mainly to the charging provisions of the statute and the machinery provisions are construed liberally.

5. **INTERPRETATION OF TAX TREATY:**

The tax treaties could either be widely interpreted by giving effect to its purpose or narrowly interpreted by strictly confining it to the literal text or wordings. The approach to interpretation of tax treaties is not the same as that of domestic laws. Domestic tax laws are generally interpreted strictly relying on the natural and grammatical meaning of the text. However interpretation of treaties is governed by Vienna Convention. An ambiguous provision in a treaty should be interpreted in accordance with the object and purpose of the treaty in question.\textsuperscript{15} Although the initial step is considering the ordinary meaning of the words of the treaty, purposivism approach is followed in case of ambiguity instead of textualism. The Supreme Court opined that the principles adopted while interpreting tax treaties are not similar to that of Statutory legislation because the provisions of international treaties are negotiated by States and entered at political level after several considerations and these are kept in mind while interpreting, whereas a statute has to be interpreted keeping in mind the well-known principles or canons of interpretation of statute.\textsuperscript{16}

Therefore interpretation of tax treaties like double taxation avoidance agreement is not similar to general interpretation of taxing statute.

\textsuperscript{13}Gursahai v CIT, AIR 1963 SC 1062
\textsuperscript{14} (2007) 1 SCC 62
\textsuperscript{15}Vienna Convention on Law of Treaties, Article 31
\textsuperscript{16}Union of India and Anr. v. Azadi Bachao Andolan and Anr, civil appeal no. 8162 of 2003
6. **CRITICAL ANALYSIS:**

It is a well-established principle that the fiscal laws are construed in strict sense. But the application of fundamental rule of construction is inevitable. The meaning and intention of the statute is gathered from the plain and unambiguous provisions of that statute. Though the taxing statutes are construed strictly, it is essential to make sure that the construction does not suffer from any vices of rigid rule of interpretation.  

Application of strict rule is reasonable, but in certain cases it might lead to absurdity. The new faceless assessment scheme of 2020 is an example. The scheme was introduced by the Central government which is empowered to issue such scheme under §143(3A) of the Income Tax Act, 1961. According to the scheme, the assessee does not have the right to personal hearing by default. The assessee can request for it and it shall be granted only if the case falls within the specified list. But according to the Provision 2(i) of the scheme, assessment includes assessment under §144 of the Income tax Act as well. If the said provision is construed in strict sense, the right to personal hearing is granted only for specific cases. However under §144 of the Income Tax Act, 1961, assessment is made only after giving the assessee an opportunity of being heard. The Income Tax Tribunal observed that it is inherent in the very nature of assessment under §144 that the assessee should be given the opportunity of being heard with respect to the materials gathered by the Assessing officer, otherwise it would be a violation of principles of Natural justice. In other words, the provisions of the scheme, if construed strictly will contradict the parent Statute. Thus the author is of the opinion that the doctrine of harmonious construction should be applied in order to remove the ambiguity or anomaly. Hence, even though strict construction is the generally applied to taxing statutes, Courts have applied rule of liberal construction in certain cases.

The Supreme Court opined that the intention of the Legislature is primarily to be gathered from the language used. Just as it is not permissible to add words or to fill in a gap or lacuna, similarly it is of universal application that effort should be made to give meaning to each and every word used by the Legislature.

Thus, pure textualist approach is not followed in all cases involving interpretation of taxing statute.

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17 K.P. Sons v. Sales Tax Officer and Anr, 1987 67 STC 38 MP
18 Supra 10
19 Harjinder Singh V. ITO, ITAT (7391) ITAT Amritsar (62)
20 Mohammad Ali Khan v. CWT
7. **COMPARATIVE ANALYSIS OF INTERPRETATION OF TAXING STATUTES IN US, UK AND INDIA:**

In United States of America, liberal construction is adopted in case of taxing statutes. The mode of interpretation in United States is different from that of India. The doctrine of judicial deference is followed by that country. According to this doctrine, the federal court defers to the agency’s interpretation of ambiguous statute if it is considered reasonable.\(^\text{21}\) The Internal Revenue Service (IRS) follows purposivism approach while the federal courts follow textualism. In other words the administrative authority is purposivist in interpreting statutes while the judicial authority is textualist during statutory interpretation.\(^\text{22}\) The liberal view supports the theory that the ultimate objective of tax measures is accomplishment of good social order and strict interpretation would result in loss of revenue to the Government.

In UK, the taxing statutes are construed strictly. The natural meaning of the text is given importance. The proper way of construing revenue legislations is to give fair and reasonable construction to their language.\(^\text{23}\) The United Kingdom has always followed the literal statutory construction since the tax legislations mostly consist of precise, specific and detailed provisions that enables strict construction.\(^\text{24}\) The Indian Courts follow the UK’s approach of strict construction with respect to the charging provisions of the taxing statute. However the other provisions are construed liberally. Thus, the Indian Courts mostly construe the taxing statute in strict sense except in few cases if it is with respect to machinery provisions.

8. **CONCLUSION:**

It can be said that rule of strict construction is generally applied to taxing statutes. Fiscal legislations, unlike penal statutes, are not fully construed in strict sense. The machinery provisions are open to liberal interpretation. Although the words or text of the provisions of taxing laws are literally construed with regard to grammatical meaning, if this literal interpretation leads to absurdity, the Golden rule of interpretation will apply. Rule of strict construction might be the primary principle applied while construing the taxing statutes, but it is not the only rule applied. If on interpretation two or more provisions contradict each other, then doctrine of harmonious construction will come into play. The author is of the

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\(^\text{23}\) Ormond Investment Co v Betts, (1928) AC 143
opinion that this doctrine should be applied while interpreting the faceless assessment scheme of 2020 since it is ambiguous and contradicts the provisions of the parent statute i.e. Income tax Act, 1961. The taxing statutes are construed strictly because it imposes a liability on a person or an entity to pay tax and if it is interpreted liberally the scope of application may get broadened thereby making a person liable to pay tax even if the legislature did not intend to tax that particular subject. It might even lead to tax evasion if the provisions are construed liberally. Hence, the courts depend mainly on the plain meaning of the text or wordings of the statute and thus rule of strict construction is primarily applied in case of fiscal laws or Taxing statutes.