



DECODING TAX STATUTES: A STRICT INTERPRETATION APPROACH

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INTRODUCTION

A tax can be termed as a compulsory contribution to the support of the Government, levied on persons, income, commodities, transactions etc. However, interpreting tax laws becomes quintessential for many reasons. Interpreting tax laws in a clear and consistent manner promotes legal certainty, which helps taxpayers understand their tax obligations and plan their affairs accordingly. Besides, the interpretation of tax laws helps to provide clarity to tax administrators and tax professionals, who can rely on the clear and consistent interpretation of the tax laws to perform their duties. Thus, the strict interpretation of taxing statutes is quintessential for promoting legal certainty, fairness, compliance, the rule of law, and clarity in tax administration.

A strict interpretation of taxing statutes refers to the approach of interpreting tax laws and regulations in a literal and precise manner. In this approach, tax laws are viewed as strict and unambiguous, and any ambiguity or uncertainty is resolved in favour of the taxpayer. This interpretation is based on the principle that taxes are the lifeblood and source of income for the Government and

should be imposed only as authorized by clear and unmistakable legislative intent.

HISTORICAL JURISPRUDENCE

The interpretation of taxing statutes has a long and complex history. The early days of the United States witnessed the federal Government relying primarily on tariffs and excises to generate revenue. However, in the late 19th and early 20th centuries, the Federal Government began to rely more heavily on income taxes as a source of revenue. This shift in taxation led to several legal challenges, as the constitutionality of income taxes was not firmly established.¹

One of the most notable cases in the history of taxing statutes interpretation is *Brushaber v. Union Pacific Railroad Co*² (1916). The Apex Court upheld the constitutionality of the federal income tax imposed by the 16th Amendment, which provided Congress with the power to tax incomes 'from whatever source derived.' This decision established the principle that the Federal Government had the authority to tax the income of individuals and corporations and laid the foundation for the modern federal income tax system.

Another important case in the history of interpreting tax statutes is the case of *Helvering v. Gregory*³ (1935). In this case, the Supreme Court established the principle of 'economic reality' as the basis for interpreting tax statutes by laying out the roots for the principle - the substance over form doctrine. The Court observed that the substance over form doctrine applies only

¹ Constitutional Rights Foundation, *The Income Tax Amendment: Most Thought It Was a Great Idea in 1913*, <https://www.crf-usa.org/bill-of-rights-in->

[action/bria-11-3-b-the-income-tax-amendment-most-thought-it-was-a-great-idea-in-1913.html/](https://www.crf-usa.org/bill-of-rights-in-action/bria-11-3-b-the-income-tax-amendment-most-thought-it-was-a-great-idea-in-1913.html/).

² 240 U.S. 1 (1916).

³ *Gregory v. Helvering*, 293 U.S. 465, 469-470 (1935).



when the transaction, prima facie, lies outside the plain intent of the legislation and, therefore, respecting the transaction would be to deprive the statutory provision in question. The Court held that the form of a transaction should not be controlling in determining its tax consequences and that the ‘substance’ or ‘economic reality’ of the transaction should be considered. Subsequently, *Frank Lyon Co. v. United States*⁴ (1978) engrained the doctrine into the US tax law regime. This principle is still widely used today in interpreting tax statutes and regulations.⁵

The judicial trend in the UK towards tax statutes, from the beginning, has been to interpret the legislation literally and to determine the words according to strict construction.⁶ Judges were formulating early approaches to interpreting fiscal statutes long before they encountered the modern revenue models. The early observations can be seen in the guise of imposition of law on stamp duties. Documents are required for stamp duties; if not, they cannot be used in judicial proceedings. Thus, it was left to the judicial discretion on their enforcement. The strict interpretation approach was enunciated by Lord Ellenbrough CJ in *Warrington v Furber*, 1809. It was observed that ‘where the subject is to be charged with a duty, the cases in

which it is to be attached ought to be fairly market out.’ Contrarily, Blackstone, in his 1809 edition, repudiated that: ‘it is considered a rule of construction of revenue acts, in ambiguous cases, to lean in favour of the revenue. This rule is agreeable to good policy and the public interests, but, beyond that, which may be regarded as established law, no one can ever be said to have an undue advantage in our courts.’⁷

Thus, it is pertinent to acknowledge that early jurisprudence, or the legal principles and precedents established in early court cases, can be highly relevant in interpreting taxing statutes. The courts' early decisions on tax laws can provide valuable insight into the legislative intent behind those laws and can serve as persuasive authority in future cases. Additionally, they can establish important interpretive rules and clarify ambiguous terms and phrases within the tax statutes.

STRICT CONSTRUCTION OF TAX STATUTES

A taxing statute must be strictly construed by which the construction only accommodates a plain meaning of the words irrespective of its consequences.⁸ This rule is well established in and reaffirmed in several cases.⁹

⁴ 435 U.S. 561, 573 (1978). See also *Commissioner v. Court Holding Co.*, 324 U.S. 331 (1945).

⁵ Freeman Law, *Is “Form” “Substance” When it Comes to Law? The Future of the Doctrines of Economic Substance and Substance Over Form*, <https://freemanlaw.com/substance-over-form-doctrine/>.

⁶ K.D. Gaur, *Judicial Attitude to Tax Avoidance in the United Kingdom and India*, https://www.jstor.org/stable/pdf/43950198.pdf?refreqid=excelsior%3A8a49fddddd435de5d45a534ae05ec184a&ab_segments=&origin=&acceptTC=1/ (1973).

⁷ Williams, David W., *Taxing Statutes Are Taxing Statutes: The Interpretation of Revenue Legislation*,

The Modern Law Review, vol. 41, no.4, pp. 404–22, *JSTOR*, (1978), https://www.jstor.org/stable/pdf/1095504.pdf?refreqid=excelsior%3A246ec76aab932713f0cd40bdd17caa36&ab_segments=&origin=&acceptTC=1/.

⁸ Tarun Jain, *Interpretation of fiscal exemptions: Another debate commences?*, 2021 SCC OnLine Blog Exp 14, <https://www.sconline.com/blog/post/2021/03/06/interpretation-of-fiscal-exemptions-another-debate-commences/>

⁹ *M Narasimhaiah v. Commr. For transport*, AIR 1988 SC 240.



Article 265 of the Constitution provides: ‘No tax shall be levied or collected except by authority of law’. In simple words, any compulsory extraction of money by the Government amounts to imposition of a tax which is not permissible except by or under the authority of a statutory provision. However, the manner in which the fiscal statutes are drafted leaves scope for conflict of interest. Consequently, the cardinal principle is that taxing statute should be construed strictly.

As mentioned earlier, the power to tax is inherently a sovereign power; therefore, no tax can be levied or collected except by the authority of a validly enacted law. A charging section imposes the levy, but no particular form or language is prescribed for a charging section. A charging section must be clearly worded without any deficiency as regards the subject or person to be taxed. If the language employed in charging section is plain or unambiguous, then even absurdity is not a consideration for deviating from the letter of law.¹⁰ Therefore, no question of strict construction arises when the charging section reasonably has only one meaning. Further, the rule of strict construction applies primarily to such provision of the statute and has no application to provisions laying down machinery for the recovery, calculation or to provisions related to tax collection.

A taxing statute must be interpreted as it stands, with no additions and no substractions, on the ground of legislative

intendment or otherwise.¹¹ It is worth mentioning the classic statement of Lord Wensleydale in *Re, Micklethwait*¹² that ‘the subject is not to be taxed without clear words for that purpose; and also that every Act of Parliament must be read according to the natural construction of its words’. Thus, the entire matter is governed wholly by the words of the provision and in such a case, the task of interpretation can hardly be said to arise: *absoluta sententia expositore non indeget*.¹³ In addition, there is no equity in taxing statute and either the subject is within it or not on the words of the enactment or the validity of the rule made thereunder. The Supreme Court in *Murarilal Mahabir Prasad v. V R Vad*¹⁴ has observed that there is no equity about a tax in the sense that a provision by which a tax is imposed has to be construed strictly, regardless of the hardship that such a construction may cause either to the treasury or to the taxpayer. Thus, as quoted by Rowlatt J, in *Cape Brandy* case ‘*There is no room for any intendment. There is no equity about a tax. There is no presumption as to tax*’. Contrarily, equitable construction may be resorted to where strict literal construction does not lead to the result intended.¹⁵

In construing a taxing Act, the Court is not justified in straining the language to hold a subject liable to tax. The Court cannot proceed to make good the deficiencies, if there be any, in the statute. Hence, it is not the function of a court of law to give words unnatural meanings to cover loopholes and must not be astute to hunt out ambiguities by an unnatural construction of taxing section.¹⁶

¹⁰ *Yeshwant Rao Ghorpade v. C.W.T., Bangalore*, (1966) 61 TTR 44 (SC).

¹¹ *VVS Sugars v. Govt of AP*, (1999) 4 SCC 192. (1885) 11 Ex 452.

¹³ *New Shorrock Spinning and Manufacturing Co. Ltd. v Raval*, 37 ITR 41 (Bom).

¹⁴ AIR 1976 SC 313.

¹⁵ *Keshavji Ravji v CIT*, 183 ITR 1(SC).

¹⁶ AB Kafaltiya, *Interpretation of Statutes*, Lexis Nexis (2d ed. 2017).



As discussed above, the Court cannot proceed to make good deficiencies in the language and will not be justified in adding words thereto. In this matter, it is also important to discuss the implications for the taxpayer in case of any ambiguity. It is now well settled that if the interpretation of a fiscal enactment is in doubt, the construction most beneficial to the subject should be adopted, even if it results in obtaining an advantage for the subject. In construing the words of a fiscal statute, if there are two possible interpretations, the effect is to be given to the one that favours the citizen and not the one that imposes a burden on him.¹⁷

Again, in a criminal trial or a quasi-criminal proceeding, the Court is entitled to consider the transaction's substance and determine the offender's liability. Nonetheless, as observed by Bhagwati J. in *A.V. Fernandez v. State of Kerala*¹⁸, in considering fiscal statute, a transaction cannot be taxed on any doctrine of 'substance of the matter' and regard has to be given to the strict letter of the law. The reason for the same is that the tax authorities are not entitled to fix tax liability on the subject on the supposed 'spirit of the law' or by inference or by analogy. In other words, plain meaning should be given effect without going into logic and common sense. However, the substance of the matter may be considered to know the economic realities or to lift the corporate veil in cases of tax evasion.¹⁹

Another important facet of strict interpretation is that words and phrases must conform to the intention of the legislature. In interpreting items and articles in taxing

statutes, resort should be had not to the scientific or technical meaning but to the meaning attached to them by those dealing in them in their commercial sense. What is relevant is not the dictionary meaning but how those entries are understood in common parlance. In *Avadh Sugar Mills Ltd. v. Sales Tax Officer*, the meaning of 'oil seeds' was not given in the Central Sales Tax Act, 1956. The SC held that in finding out the true meaning of the term, dictionaries ought not to be referred to instead, their meaning should be ascribed to the term found in commercial parlance.

INTERPRETATION OF EXEMPTION PROVISIONS

An exemption provision grants exemption from tax payment on certain specified income or goods and services under specific conditions and have to be strictly construed.²⁰ Thus, interpretation of such provisions primarily refers to understanding and applying the provisions related to exemptions from tax payment. It is a well-known principle that a person who claims an exemption has to establish it and the rule of strict construction does not negate its application. The interpretation is important as it determines a taxpayer's tax liability and helps avoid disputes and litigation related to taxes.

The exemption provision cannot be unduly extended to produce unintended results in derogation of the plain language.²¹ Its provisions and notifications issued under a taxing statute are to be strictly construed. The benefit of doubt, if any, should be construed

¹⁷ C.A. *Abraham v. I.T.O. Kottayam*, AIR 1961 SC 609.

¹⁸ AIR 1957 SC 657.

¹⁹ C.I.T. v. *Meenakshi Mills*, AIR 1967 SC 819.

²⁰ *Oxford University Press v. CIT*, AIR 2001 SC 886.

²¹ *CCE v. Modi Rubber Ltd.*, (2002) 1 SCC 5.



in favour of the assessee or taxpayer.²² However, this established view was unsettled in the case of *CC v. Dilip Kumar & Co*²³. It was observed that the burden to prove tax exemption under a notification is on the assessee and the notification must be construed strictly. In case of any ambiguity in such provisions, the benefit cannot be claimed by the assessee and must be construed in favour of the revenue.

Contrarily, it is important to note that liberal interpretation should be applied to exemptions made with a beneficent object, for example, exemption is given for the purpose of developing urban or rural areas for the public good, to give incentive to the co-operative movement, permitting concessional rates of tax for encouraging an industrial activity, exemptions for encouraging investment in new machinery or plant etc.²⁴

In *Associated Cement Companies Ltd. v. State of Bihar*²⁵, the Apex Court held that an exemption provision, on normal principle of construction, is construed strictly either because of legislative intention or on economic justification of inequitable burden of progressive approach of fiscal provisions intended to augment State revenue. However, once the exemption becomes applicable, no principle or rule requires to be construed strictly. It went on to substantiate that strict and liberal construction of an exemption provision is to be invoked at different stages of interpretation. When the question is whether an assessee falls within the notification or the exemption clause, it can be construed strictly against the assessee.

Nonetheless, once ambiguity or doubt about applicability is lifted and the subject falls within the ambit of the notification, then full play should be given to it and it calls for a wider and liberal construction.

LIBERAL CONSTRUCTION OF FISCAL STATUTES

A liberal interpretation of taxing statutes refers to an approach where the tax laws are interpreted in a way that favours the taxpayer and allows for a broader application of exemptions, deductions, and credits. This interpretation aims to reduce the tax burden on taxpayers and ensure that they are only taxed in accordance with the clear intent of the tax legislation. A liberal interpretation can also help to avoid harsh and unjust outcomes that may result from a strict and literal application of the tax laws. It is important to note that while a liberal interpretation may be favoured in some cases, it should still be consistent with the overall purpose and language of the tax statutes.

Insofar as taxing statutes are concerned, unduly liberal construction should be avoided. When words acquire a particular meaning or sense because of their authoritative construction by superior courts, they are presumed to have been used in the same sense when used in subsequent legislation in the same or similar context²⁶. While literal construction is the general rule, it does not mean that it should be adopted even if it leads to a discriminatory or incongruous result. Where literal interpretation leads to a result not intended to

²² *Union India v. Kanunga Industries* (1992) 2 SCC 56.
²³ (2018) 9 SCC 1.

²⁴ *Commissioners of Wealth Tax Ap v. Officer in charge (Court of Wards), Paigah*, AIR 1977 SC 113.

²⁵ (2004) 7 SCC 642.

²⁶ *Keshavji Ravji & Co. v. CIT*, (1990) 2 SCC 231.



subserve the object of the legislation, another construction in consonance with the object should be adopted.²⁷

The purpose of all rules of interpretation is to give effect to the object of the enactment, having regard to the language used. However, as held in *CWS (India) Ltd. v. CIT*²⁸, the provisions granting incentives for promoting economic growth and development should be liberally construed. Thus, interpretation cannot be a mechanical exercise.

CONCLUSION

In conclusion, interpreting Indian tax statutes is a complex process that requires a thorough understanding of the legal provisions, judicial precedents, and administrative practices. The Indian tax system is characterized by its intricate provisions, which often pose challenges for taxpayers and tax authorities alike. A proper interpretation of tax statutes is crucial for ensuring that the tax system operates fairly and equitably. Moreover, it helps taxpayers understand their obligations and rights and minimizes the scope for disputes.

The courts play a crucial role in interpreting tax statutes and resolving disputes between taxpayers and tax authorities. Over the years, the judiciary has developed a rich body of case law that provides guidance on the interpretation of tax statutes. However, the courts' approach to tax interpretation is not uniform, and there are instances where conflicting judicial precedents exist.

In conclusion, the interpretation of Indian tax statutes is a dynamic and evolving process

that requires a deep understanding of the legal, economic, and administrative aspects of the tax system. The continued growth and development of the Indian economy, coupled with the increasing complexity of tax provisions, highlights the need for ongoing efforts to simplify the tax system and provide clarity on the interpretation of tax statutes.

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²⁷ Ibid.

²⁸ 1994 Supp (2) SCC 296.