SPECIAL BENCH.

Before Sir Walter Salis Schwabe, Kt., K.C., Chief Justice, and Mr. Justice Coutts Trotter.

BOARD OF REVENUE, REFERRING OFFICER,

v.

MUNISWAMI CHETTI AND SONS (ASSESSEES).*

1923, February 22, and August 28.

Indian Income-tax Act (VII of 1918), sec. 9 (2) (ix)—A trading on his own account and also as partner in a firm—Gain in one and loss in another—Right to set off loss against gain—Charges incurred to ascertain taxable profits—Right to deduct charges from income.

A who traded on his own account held as part of his business a share in a firm consisting of himself and *B*, whose business was to deal in similar goods and was subsidiary to *A*'s. In a certain year *A* made a profit in his own business but sustained loss as a partner.

Held, that in arriving at the taxable income of *A* for the year his loss as a partner could be set off against his gains in his own business.

Held further, that in arriving at the taxable income of *A* for a particular year, charges and costs incurred by him in employing accountants and lawyers in connexion with a dispute between him and the Government as to the amount of excess profits duty payable by him for a previous year, could not be deducted from the gross income, since such charges and costs were not expenditure within the meaning of section 9 (2) (ix) of the Income-tax Act, VII of 1918, incurred solely for the purpose of earning such profits but were charges incurred after the profits were earned. *Inland Revenue Commissioners* v. *Warnes & Co.*, [1919] 2 K.B., 444, and *Ward & Co.* v. *Commissioner of Taxes* [1923] A.C., 145, followed.

CASE stated under section 51 (1) of the Income-tax Act, VII of 1918, by the Secretary, Board of Revenue, Madras.

The facts appear from the Opinion of the High Court.

R. N. Aiyar with *O. T. Govindan Nambiyar* for assessee.—On the first question:—If one person carries

* Referred Case No. 19 of 1922.

BOARD OF REVENUE v. MUNISWAMI CHETTI.

on two businesses, loss in one can be set off against gain in the other. Both are his *businesses* and income from both must be treated as from one and the same source, viz., "business" for purposes of income-tax. He is only one "assessee" within the meaning of the Income-tax Act though carrying on two businesses, one in his individual capacity and the other as partner. Profits from "any business" in section 9 (1) (*B*) of the Act, means profits from one or many businesses. He referred to Konstram's Law of Income-tax, page 173, and rule 13 of Schedule D of the English Income-tax Act of 1918. Though there is no specific provision in the Indian Act on this point, the definitions of "assessee," "income" and "business" in the Act make this clear. On the second question:—Section 20 of the Excess Profits Duty Act (X of 1919) allows a deduction of such duty when paid, from assessable income for purposes of income-tax. Hence all charges incurred by the assessee in proving to the Government by engaging accountants and lawyers as to what exactly was his income for purposes of Excess Profits Duty Act and Income-tax Act must be deducted from gross income as being proper charges.

Government Pleader (C. V. Anantakrishna Ayyar) for the Crown.—On the first question:—Losses in one business cannot be set off against gains in another. If there is a loss in one business that business cannot be taxed, but that fact cannot have the result of reducing the taxable income of the other business, for the Act allows set off only in certain cases and this is not one of them. Moreover if one trades both in his individual capacity and also as a partner of a firm he has two separate entities. Also if the businesses are distinct and not connected with each other there cannot be a set off. On the second question:—Charges and costs cannot be

deducted as they are not expenditure incurred for earning the profit and as they were incurred after the profits were earned; see section 9 (2) (ix); see *Inland Revenue Commissioners* v. *Warnes & Co.*(1) and *Ward & Co.* v. *Commissioner of Taxes*(2), *Strong & Co., Limited* v. *Woodifield*(3), *Inland Revenue Commissioners* v. *Von Glehn*(4). Moreover Excess Profits Duty Act applied only for one year and allowed deduction of such duty paid only in adjustments made before 31st March 1920 and as in this case the adjustment was made in later years (i.e.) 1921–1922 the payment cannot be deducted; see *The Chief Commissioner of Income-tax, Madras* v. *The Eastern Extension Australasia and China Telegraph Co., Ltd.*(5).

JUDGMENT.

SCHWABE, C.J.

SCHWABE, C.J.—This case is referred under the Income-tax Act by the Board of Revenue for the opinion of the High Court. The question relates to the assessment for income-tax of the firm known as B. Muniswami Chetti and Sons and there are two distinct points referred.

(i) B. Muniswami Chetti and Sons carry on a business in piece-goods, the partners in the firm being B. Damodaram Chetty and P. V. Ramanujam Chetty, Damodaram Chetty having a much larger share. On the facts as now found it is clear that that firm engaged in business with other partners in two other firms, one called the Carnatic Import Company and the other B. Damodaram Chetty & Co., whose business were of an allied character in that they dealt in goods similar to those dealt in by Muniswami Chetti and Sons. B. Munisami Chetti and Sons had a much larger share in those

(1) [1919] 2 K.B., 444. (2) [1923] A.C., 145.
(3) [1906] A.C., 448. (4) [1920] 2 K.B., 553.
(5) (1921) I.L.R., 44 Mad., 489.

BOARD OF REVENUE v. MUNISWAMI CHETTI.

SCHWABE, C.J.

other two firms there being in each case a partner with a small share to encourage him to take a real interest in the management of the business. In the year of assessment B. Muniswami Chetti and Sons made a profit and the other two firms made a loss. B. Muniswami Chetti and Sons claim that they are entitled, for the purpose of assessment, to set off their share of the loss in the other two firms against the profit made in their own firm. The Crown contends, on the other hand, that they must be treated separately and must pay income-tax on the profit of their firm, and that the only effect of the loss of the other two firms would be that these firms would not have to pay income-tax. In our judgment, the determination of this question depends upon whether it is a fact that the business of B. Muniswami Chetti and Sons is being carried on in part by engaging with partners in the other firms. Where the subsidiary business engaged in is connected with the main business, and is a proper employment of the assessee's capital or labour, it is, in my judgment for the purpose of assessment, to be treated as part of the business of the firm. If the firm in one branch makes a loss, that loss may be set off against the profits made in its head office or other branches. Applying that test to this case I think it is clear that the contention of the assessee is right and that B. Muniswami Chetti and Sons are entitled to have their assessment arrived at by taking into account the loss made by them in the other two firms.

(ii) They claim also in arriving at their profits for the tax year, 1921–1922, to deduct certain expenditure incurred by them (*a*) in employing accountants and lawyers in the matter of dispute between them and the Government as to the amount of excess profits duty payable by them for the year ending March 1920, the year in which the Excess Profits Duty Act applied and

(*b*) similar expenses incurred by them in arriving at the income on which income-tax assessment was made or was to be made. These expenses are perfectly proper expenditure by the company of the company's money, but whether they can be brought into account in arriving at the proper assessment of the income-tax must depend upon the construction of section 9 (2) (ix) of the Income-tax Act of 1918 which runs as follows :—

> "Such profits shall be computed after making the following allowances, in respect of sums paid, namely, in respect of any expenditure (not being in the nature of capital expenditure) incurred solely for the purpose of earning such profits."

In my judgment these monies were expended not for the purpose of earning profits at all but for the purpose of, in one case, protecting profits from Government's claim to income-tax and in other cases of getting back from Government the excess profits duty claimed by or paid to the Government in respect of some past period. The words of this rule are much the same as the words of the rule in Schedule D of the Income-tax Act of 1918 in England and of the rule in the Income-tax Act current in New Zealand, and there have been cases both in England, and in the Privy Council on appeal from New Zealand which indicate the view of the English Courts which is to the effect that these and similar words are to be construed strictly, by ascertaining whether or not the expenditure was for the sole purpose of earning profits. So the amount paid to the Government in the nature of a fine arising out of a matter connected with the business and costs incurred in resisting the imposition of such fine were held in *Inland Revenue Commissioners* v. *Warnes & Co.*(1) not to be charges that could be deducted. In *Ward & Co.* v. *Commissioner of Taxes*(2) their Lordships of the Privy Council held that no deduction could be made for

(1) [1919] 2 K.B., 444. (2) [1923] A.C., 145.

BOARD OF REVENUE v. MUNISWAMI CHETTI.

SCHWABE, C.J.

monies spent by a company in printing and distributing literature directed against prohibition, which expenditure was admitted to be in the interest of the preservation of the assessee's trade. We were referred to the Excess Profits Duty Act, X of 1919, section 20, and it was suggested that because the amount of the excess profits duty is to be allowed as a deduction in respect of the profits of a business for the purpose of income-tax therefore the costs of arriving at the excess profits duty must also be so allowed. It is clear on an examination of the section that this has got to be for a specified year and does not apply to any later year ; nor do I think that apart from that limitation the fact that the excess profits duty is by statute allowed to be deducted would make the costs of arriving at the excess profits duty also a deduction. If the statute had desired to make it so, it would have been quite simple to have stated that the excess profits duty and any money expended in arriving at the right amount of excess profits duty shall be a deduction for the purpose of income-tax. The section does not say so and I see no reason why it should be implied.

I have come to the conclusion that on the first point the contention of the assessee is right and on the second wrong.

The first point is the main and the more important point and I think that the assessee must have his costs of this reference except in so far as they have been increased by adding a claim on the second point. Costs in this case will be taxed on the Original Side scale.

I think that it would be desirable at some future time on a suitable occasion with the assistance of the Vakils' Association, if they choose to assist in this matter, to consider the question of the taxation of costs, with a view to framing some rule or establishing some definite practice in such matters.

COUTTS TROTTER, J.—Now that we have unambiguous findings, I do not entertain the slightest doubt about the first point which seems to me almost too plain for discussion. Indeed when Mr. Ananthakrishna Ayyar came to develop the argument, it was clear that the only way in which he could contend for the claim made by Government was by arguing that under section 9 (1) of the Income-tax Act of 1918 the profits of any business carried on by him, that is, the assessee, have to be expanded into profits of any business carried on by him solely so as to exclude any business that he may carry on in conjunction with others. Here we have a company part of whose business is to hold a share in a separate business. It takes this share in the course of its own business and it receives whatever profit it receives or loses whatever it loses in the course of its own business.

With regard to the second point, I feel more doubt. The section occurs in many Acts of many countries and Mr. Justice ROWLATT, a Judge of great experience and learning in revenue matters, has frankly said that he does not see his way to give a general definition of the true construction of the section but that he is content to say about each case as it comes along whether in his view it falls within the section. This seems to me a difficult case, more difficult than the one which that learned Judge had to deal with. I do not think that the expenses incurred here can be said, in any sense that a plain man would understand, to be correctly described as expenditure incurred for the purpose of earning profits. It seems to me that the expenditure was incurred after the profits had been earned. That appears to be sufficient to take the case out of the section.

I agree to the order as to costs.

N.R.