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regards joint property in a Hindu family must apply, and that when one trustee dies the members of the joint family will take the trusteeship according to the law of survivorship. That will exclude the claim put forward by the plaintiff who is only a female member of the joint family. I therefore agree with my learned brother in thinking that the Subordinate Judge was right in the view he has taken of this case and that the plaintiff's appeal fails and must be dismissed with costs.

K.R.

APPELLATE CIVIL.

Before Sir Murray Coutts Trotter, Kt., Chief Justice and Mr. Justice Krishnan.

1925, January 22.

COMMISSIONER OF INCOME-TAX, MADRAS, REFERRING OFFICER

v.

CHENGALVARAYA CHETTI AND ANOTHER, ASSESSEES.*

Income-tax Act XI of 1922—*Trade gain or loss in each year—Method of calculation.*

If the market value of certain goods bought by a trader in the beginning of a certain year gradually becomes lower than the cost price during the course of the year and the trader therefore submits an income-tax return showing that his trade had a loss during that year and gets exemption from tax for that year from the authorities who accept the market value as put by him, the value that the trader should put for the opening balance of his remaining stock in trade at the beginning of the next year is not their original cost price but the lower market value accepted by the authorities as ruling at the end of the previous year. If on the basis of such lower valuation there is a profit at the end of the second year, the trader must pay

* Referred Case No. 16 of 1924.

income-tax on such profit, though taking both the years together there might be a net loss in trade at the end of the second year.

Income-tax for a particular year is calculated upon a proper estimate of profit and loss only of that particular year.

CASE stated under section 66 (3) of the Indian Income-tax Act by D. N. Strathie, Commissioner of Income-tax, Madras, in his letter No. 1414, dated 15th October 1924, in pursuance of the Order of the High Court, dated 15th August 1924, on the Mandamus application of S. Chengalvaraya Chetti and S. Munusami Chetti.

The facts of the case are as follows :—The assessees who were trading in certain piece-goods bought yarn and caused country cloths to be made out of them in the year 1921. For the twelve months ending 12th April 1922 they submitted an Income-tax return in which they put the cost price of each piece of cloth at the beginning of the year at Rs. 13–8–0 and the selling price at the end of the tax year at Rs. 6 a piece. This account was accepted by the income-tax authorities who levied no tax on the assessees in that year as their accounts showed a loss. Then in the return submitted by the assessees for the next twelve months ending 12th April 1923, the assessees calculated the value of the stock in trade remaining on 13th April 1922, at Rs. 13–8–0 a piece, and on that basis showed a loss at the end of the second year also, though the market value of each piece was Rs. 8–8–0 at the end of the second year. The income-tax authorities claimed that the value to be put on the opening balance of the remaining stock in trade at the beginning of the second tax year should be Rs. 6 a piece and not Rs. 13–8–0 and that as the assessees derived a profit on that basis at the end of the second year they should be assessed on that profit. The assessees' answer to this claim was that taking the transactions even of the two years together the trade

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ended in a loss. As the assessees' request to the Income-tax authorities to state a case to the High Court under section 66 of the Income-tax Act, XI of 1922, was not complied with, the assessees filed a petition for a Mandamus in the High Court to call upon the income-tax authorities to state a case to the High Court. On that petition, His Lordship Mr. Justice KUMARASWAMI SASTRIYAR ordered the Income-tax authorities to state a case for the decision of the High Court under section 66 (3) of the Act. While making the order, His Lordship framed the following question of law as arising in the case and asked the Income-tax authorities to submit their opinion on the points arising in the question of law so framed. The question so framed is as follows:—

"Whether where a man has been carrying on one business which is a losing concern and he had not sought to set off loss against any other business he carries on which ended in a profit and no such advantage has been obtained, the mere fact that for the purpose of showing that he has made no profit for the year he gave the market value at the close of that year should be deemed conclusive against him even though he got no advantage by the form in which he has submitted his income-tax return and whether he should be deemed to have made a large profit while as a matter of fact he has incurred a large loss."

In forwarding their statement of the case and their opinion on the points arising on the question of law, the Income-tax authorities adhered to their opinion that the assessees should value their opening balance of the stock remaining at the beginning of the second year at Rs. 6 a piece and that they were rightly assessed for that year as having made a profit.

M. Patanjali Sastri for the Commissioner of Income-tax.

A. Suryanarayanayya for the Assessees.

JUDGMENT.

COUTTS TROTTER, C.J.—This is a case in which my learned brother, KUMARASWAMI SASTRI, J., directed the Commissioner of Income-tax to state a case for the opinion of the High Court under section 66 of the Income-tax Act.

The learned Judge did something further which the section does not provide for; he framed the question which he supposed to arise from the facts as set out in the Commissioner's report. With great respect to the learned Judge, I do not think that the question he framed was the real question raised in the case, and I think that the question as he has framed it is so beset with assumptions and begged questions that it would be impossible to decide fairly what the real point in this case is by any answer that could be given to the highly involved question he formulated.

The facts here are very simple. The assessees are a firm of piece-goods merchants in this City and they keep their books and render their accounts to the income-tax authorities in what is known generally as the mercantile system of accounts. It is obviously a very rough and ready method; but it is the one that they have adopted and the one that the income-tax authorities are prepared to accept (provided they are satisfied with the honesty of the items set out) as giving sufficiently, for practical purposes, an accurate figure on which they can assess income-tax. The method is this: You set out on the debit side your opening stock and add to that the purchase of stock made during the year, you then set out on the contra side of the account the sales during the year and then you add to that the value of the stock on hand at the close of the year. Then, of course, you add to the debit side the establishment charges and the interest, if any,

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paid to creditors and so forth during the year. I should add that the accepted rule is that the assessee in crediting the closing stock figure is to take either the cost price or the market value whichever be the less—a provision obviously intended to be in favour of the trader and which enables him more evenly to distribute his loss.

Now for the year April 1921–22 an account was rendered on that footing and it showed a trading loss during the year of one lakh and accordingly these people were not assessed to income-tax at all. The loss arose in this way; they started their year with 12,570 pieces which were valued at what no doubt was taken to be the cost price, viz., Rs. 13–8–0 a piece, and at the end of the year there was left on their hands a balance of 7,573 pieces, and in accordance with the then market rate, those pieces were valued down to Rs. 6 a piece. The result was a trading loss of just over a lakh and I ought to remark, because it has a bearing on what I am going to say later, that if those goods had been put down at Rs. 13–8–0 a piece, their cost price, there still would have been a trading loss of some Rs. 45,000; so that the assessees really stood to gain nothing if the figure of Rs. 6 was an undervaluation. Now comes the next year. In that year they start off their debit side to stock on the 13th of April 1922, 7,573 pieces at Rs. 13–8–0 a piece by which means they work out a loss of Rs. 15,000 and odd. The contention of the income-tax authorities is that the stock on the opening of the account must be put at the same value as it was put as stock left on hand on the other side of the previous year's account. That seems so obvious that one must scrutinize carefully what is said against it.

The question framed by the learned Judge ends up with the statement

"Whether he should be deemed to have made a large profit, while, as a matter of fact, he has incurred a large loss."

That begs so many questions that I really hardly know how to deal with it. The question is not whether a man has made a loss from the beginning to the end of his dealings with certain goods, but whether he has made a loss or a profit during the current year's trading, having regard to how he started and how he ended up. Of course, if you had to take it, that he could go on year in and year out writing off all this loss against the cost price, no matter how old the pieces left on hand you might reach almost any result. What he does is this. He writes down at the end of the year his goods at the value at which they stand in the market, as he had to adopt the system of account in vogue. That gives him in certain cases a benefit—there is always a provision, which is intended for his benefit, that his losses in other branches can be set off. The principle, if it can be called a principle, contended for by the assessee would enable him, having cut his loss in one year, to go on claiming to deduct the same loss year in and year out and I cannot illustrate the absurdity of that better than by the hypothetical case that I put in the course of the argument. Supposing in the year 1921–22 the assessee had underwritten his loss with a firm of underwriters—I believe there are underwriters who will guarantee trading losses—and at the end of the year he goes to his underwriters and says:—"I bought at Rs. 13–8–0 a piece; this stock was worth Rs. 13–8–0 a piece at the beginning of the year; it is now worth Rs. 6; Rs. 7–8–0 is my loss; please pay me Rs. 7–8–0; I do not know what defence the underwriters would have to that claim. Suppose that he goes again next year to the underwriters with the same purpose of having his trading loss underwritten, what are the

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underwriters going to say if he says that the value of the same stock is Rs. 13-8-0 a piece? The underwriters would say; we paid you yesterday a partial loss on the footing that these goods had deteriorated to Rs. 6 a piece now you again value them at Rs. 13-8-0; of course, the first observation is that no underwriter would accept such a valuation. If through accident or misapprehension as to the identity of the goods, he got a second policy, and sued upon it, the defence of the underwriters would be "gross over-valuation," and to that defence it seems to me that the assured has no answer. He would be getting more than an indemnity. I cannot see that the principle is in the least different because you are dealing between the trader and the Government instead of between the trader and his underwriters. The question is, what in the proper mercantile sense is his loss or profit in the year? Appeals *ad miseri cordiam* are beside the point. The question is not so much of law but of business common sense. But there is a principle involved which determines the legal position, and I think the answer is clear that, as the value of the stock on the 13th of April 1922 was in fact and in truth Rs. 6 a piece, the assessee is not entitled to reduce what are truthfully called his profits by putting the fictitious value of Rs. 13-8-0 a piece on the stock-in-trade merely because that was the sum he happened to pay for it before the year of assessment. In my opinion, to allow this to be done would be to let the assessee ascertain not his profit or loss, but to debit himself with the same loss on the same goods *in toto* for perhaps a course of years. That cannot be permitted. If these goods had been valued at Rs. 6 and the market had gone down to say Rs. 4 he would of course be entitled in this trading year to treat the difference between Rs. 6 and Rs. 4, i.e., Rs. 2 as another loss justly debited to this year. But

in the event of the price going up above the market rate at the beginning of the year which we must take as an accurate valuation, the difference is his profit.

In our opinion, the answer that we should return to the question is that the assessee, having elected in the previous year to value his stock at the market price of Rs. 6 a piece for the purpose of showing his trade loss during that year, is not entitled in the succeeding account to revert to the purchase price figure as representing the value of the goods, but is bound by the market price which he has fixed and been assessed on in the previous year unless he can show that he made a mistake as to the market value. Perhaps the simplest way of putting it is to say that the trader made a profit in this year, but it was not a profit sufficient to compensate him for his loss in other years.

Each party will bear his own costs in this Court. Costs in the lower Court will be paid by the assessee to the Government as directed by the learned Judge; Vakil's fee Rs. 50 (Rupees fifty).

KRISHNAN, J.—I agree with what has fallen from my Lord the learned Chief Justice in this case except that I would add that the learned Judge who made the reference was not wrong in stating what in his opinion was the question of law that should be considered in this case, for a reference can be directed only on a point of law. It is difficult, however, to understand what exactly the learned Judge thought should be decided in this case. The question stated by him is put in such a form that, taking the hypothesis involved in it, it is impossible to give any answer except in the negative. That is not a fair way of framing a question. It should be so framed as to leave to the Court which afterwards hears the reference to decide the matter on the facts

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stated by the Commissioner of Income-tax who makes the reference.

The particular case before us is a very simple one. The assessee had a large stock of piece-goods, 12,570 pieces, at the beginning of 1921 which he says he bought at Rs. 13-8-0 per piece. At the end of the year the value of these goods fell in the market to Rs. 6 per piece according to his own statement. In submitting his statement to the income-tax authorities for the year April 1921 to March 1922 (Exhibit A) he has taken into account the falling price in the market for the whole stock in calculating his loss for the year though he had not sold all the stock. He has treated the remaining stock in his hand at the end of the year, 7,573 pieces, as being worth only Rs. 6 a piece and on that footing he has estimated his loss. In the next year instead of taking that stock as being worth Rs. 6 at which he valued it the day previous to the beginning of the year he valued it at Rs. 13-8-0 again and on that footing he has estimated his loss. He contends before us that, in fact, he made no profit over the transaction taken as a whole, that is, out of the 12,570 pieces he purchased, if the total selling value which he realized is taken into consideration, he has really lost money. That may be so. The question is whether we ought to take that into consideration and hold that though he had in his statement of account for the previous year elected to treat his loss on the whole of the 12,000 and odd pieces by the fall in the market price as a loss that occurred that year he should be allowed again to say the next year that the real loss occurred on the balance stock when that stock was sold that year. I do not think he can be allowed to do so. The learned vakil argues that if the loss which his clients had incurred on the sale of the goods be split up and only the loss incurred on the stock which

he sold in the year 1921 had been taken for the purposes of the statement for that year, he would still have made a loss for that year and the income-tax authorities would not have been able to levy any tax on him. That may be so, but we cannot take it into consideration at all. Having elected to treat his loss as having occurred in the year 1921–22, he cannot be allowed to treat it again as a loss in the next year also. It will not do to allow him to re-open the previous return and newly distribute the loss between the two years. It may be an advantage to do so in this case, but it would more often be a disadvantage to the assessee to do so. Having been allowed to treat his loss as one on the stock in hand the previous year, he cannot be allowed again to treat it as a loss on the sales in respect of the same stock the next year. That is the only point that really arises in this case. I entirely agree with the learned Chief Justice in the answer that he has proposed to give to the income-tax authorities that we consider that they were right in treating the second year's statement as erroneous in putting Rs. 13–8–0 as the initial value of the stock he had on hand and that he was only entitled to put Rs. 6 as the value of that stock. This is not a case really of the assessees having made no profit for the second year, for that entirely depends upon how the calculation is made. If he starts the second year with stock worth Rs. 6, the value he has put on it at the end of the previous year and if he sell it at Rs. 8–8–0 as he seems to have done, there is manifestly a profit.

N.R.