SPECIAL BENCH.

Before Sir Owen Beasley Kt., *Chief Justice,*
Mr. Justice Ramesam and Mr. Justice Cornish.

1932, January 5.

THE COMMISSIONER OF INCOME-TAX, MADRAS,
PETITIONER,

v.

MESSRS. K. SIDDHA GOWDER AND SONS
(ASSESSEES), RESPONDENTS.*

Indian Income-tax Act (XI of 1922), *ss.* 10 (2) (*iii*) *and* 24—*Capital loss—Trading loss or—Dissolution of partnership—Distribution of assets and liabilities on—Interest paid on liabilities—Deduction of, from taxable income—Right to—More businesses than one carried on by an assessee—Loss sustained by him in one or more of—Set off of, against gains and profits of other businesses—Right of—"Profits or gains of any business carried on by him" in section* 10 (1) *—Meaning of.*

The petitioners, who constituted a joint Hindu family, carried on a money-lending business. They had also a share in two firms doing other classes of business. Those two firms were dissolved, an account was taken of their assets and liabilities and those assets and liabilities, when ascertained, were distributed between the petitioners and another partner. Those liabilities represented capital borrowed entirely for the purpose of the two firms and the said borrowed capital was raised by those firms from third parties and not from any of the petitioners' businesses and was actually utilized in those two partnership businesses. During the year of account the petitioners paid interest on the liabilities of the two firms so taken over by their family.

Held that the amount paid by the petitioners for interest on the liabilities of the two firms taken over by them was not a trading loss within the meaning of section 24 of the Income-tax Act of 1922 and that the petitioners could not claim a deduction of that amount from the profits made by them in their joint family money-lending business.

* Original Petition No. 167 of 1931.

The property of the two businesses was distributed after their dissolution; and it was capital.

Where more businesses than one are carried on by an assessee, what has to be ascertained is whether they have resulted in a profit or whether one or some of them have resulted in a profit and others in a loss. If it is discovered, on an account taken in accordance with section 10, that there has been a loss in one or more of them, that loss can be set off under section 24 against the profits and gains of other businesses of whatever description.

Quaere—whether the words "profits or gains of any business carried on by him" in section 10 (1) mean "profits or gains of each and every business" carried on by him.

Commissioner of Income-tax, Madras v. *Suppan Chettiar*, (1929) I.L.R. 53 Mad. 702 (S.B.), approved.

Commissioner of Income-tax v. *Arunachelam Chettiar*, (1923) I.L.R. 47 Mad. 660 (S.B.), doubted.

REFERENCE to the High Court under section 66 (2) of the Indian Income-tax Act (XI of 1922) in the matter of K. Siddha Gowder & Sons—Ootacamund Circle—Ootacamund.

S. Doraiswami Ayyar (*with him M. R. Venkataraman and K. Nanjundiah*) for assessees:—Where more businesses than one are carried on by an assessee the loss incurred by him in one of such businesses can be set off against his profits in the other business or businesses; see *Commissioner of Income-tax* v. *Arunachelam Chettiar*(1). The real basis of the decision in that case is that, in the case of a person carrying on more businesses than one, the real mode of ascertaining his taxable income is to take into account the profits and losses of all the businesses put together. That decision is authority also for the view that for the purposes of such a case the fact that the businesses are totally distinct businesses is immaterial. *Commissioner of Income-tax* v. *Arunachelam Chettiar*(1) goes further than *Commissioner of Income-tax, Madras* v. *Suppan Chettiar*(2) in conceding the right of set off even in a case where the different business is not the individual business of the assessee but is only a partnership business. *Karam Ilahi Muhammad Shafi* v.

(1) (1923) I.L.R. 47 Mad. 660 (S.B.). (2) (1929) I.L.R. 53 Mad. 702 (S.B.).

COMMISSIONER OF INCOME-TAX, MADRAS v. SIDDHA GOWDER AND SONS.

Commissioner of Income-tax, Delhi(1) referred to in *Commissioner of Income-tax, Madras* v. *Suppan Chettiar*(2) takes the same view as that taken in *Commissioner of Income-tax* v. *Arunachelam Chettiar*(3).

[It seems to have been conceded by the Government Advocate in that case that the profits and losses of all the distinct businesses might be put together for the purpose of ascertaining the income of the assessee.—CHIEF JUSTICE.]

The assessee in the present case is entitled to deduction even in respect of Rs. 2,200 paid for interest after date of dissolution. It is not necessary that, to entitle the assessee to a right of set off, the business in which loss was incurred should actually be carried on in the year of account. *Arunachalam Chetty* v. *Commissioner of Income-tax*(4) lends support to this contention, though the facts of that case are not on all fours with those of the present. It is enough if the money in respect of which interest was paid was capital borrowed for the purpose of the business. The words "capital borrowed for purpose of business" in section 10 (2) (iii) must be held to mean capital borrowed for the purpose of the business the subject of assessment whether that business was in fact carried on or not in the year of assessment. *Arunachalam Chetty* v. *Commissioner of Income-tax*(4) gives that extended meaning to the expression. Though in that case the businesses were in fact branch businesses, that is not a necessary condition of the applicability of the principle laid down therein.

M. Patanjali Sastri for Commissioner of Income-tax.—After the dissolution of a firm and the allotment of profits and losses to the partners, what comes to each of the partners is not profit or loss as such but capitalized asset or capitalized liability; see *Inland Revenue Commissioners* v. *Burrell*(5). The accounts of the firm cannot be gone into for the purpose of ascertaining which portion of the amount allotted to a partner at the dissolution represented capital and which portion represented profits. A firm cannot be assessed as such if it is dissolved before the end of the year of account. In such a case each of the partners may be liable but not the firm as such. The liability taken over by one of the partners on dissolution is a

(1) (1929) I.L.R. 11 Lah. 38.
(2) (1929) I.L.R. 53 Mad. 702 (S.B.).
(3) (1923) I.L.R. 47 Mad. 660 (S.B.).
(4) (1928) I.L.R. 52 Mad. 296 (S.B.).
(5) [1924] 2 K.B. 52.

capital loss and interest paid thereon in the year of account is not deductible. The question whether the interest accrued due before or after the dissolution is immaterial, though, if the firm were a going concern, the amount paid for interest would be deductible under section 10 (2) (iii). All the liabilities allotted to the present assessee were incurred by the firm before the year of account. *Commissioner of Income-tax, Madras* v. *Suppan Chettiar*(1) was a case concerning the same business and is therefore distinguishable. *Commissioner of Income-tax* v. *Arunachelam Chettiar*(2) overlooks section 14 of the Act. Under that section a partner can be assessed only if the firm is not assessed. The Act recognizes the firm as an assessable unit and this circumstance has been overlooked in *Commissioner of Income-tax* v. *Arunachelam Chettiar*(2). The correctness of that decision has been questioned in *Ballarpur Collieries* v. *Commissioner of Income-tax, C.P.*(3). In the case of an unregistered firm, the firm is the assessable unit and the individual partners are ignored altogether.

K. Nanjundiah in reply.—*Inland Revenue Commissioners* v. *Burrell*(4) was a case of super-tax. Income-tax was assessed in the first instance and the question raised was one as to super-tax. Further the case was one of liquidation of a company and the principles applicable to such a case are inapplicable to the case of dissolution of a firm or to the case of a man closing up one branch of a firm. Though the firm is in fact closed it must be deemed to continue for the purposes of the Act till the liabilities of that firm are discharged.

JUDGMENT.

BEASLEY C.J.—The Commissioner of Income-tax has referred the following question to us :— BEASLEY C.J.

"Whether on the facts of this case the sum of Rs. 6,967 being the interest on the liabilities allotted to the share of the petitioner-family on the dissolution of the two firms in which it was a partner is allowable as a deduction against the profits and gains of the businesses carried on by it on its own account during the year of account."

The facts with regard to this matter can be shortly stated. The petitioners constitute a Hindu undivided

(1) (1929) I.L.R. 53 Mad. 702 (S.B.).
(2) (1923) I.L.R. 47 Mad. 660 (S.B.).
(3) (1929) 4 I.T.C. 255.
(4) [1924] 2 K.B. 52.

COMMISSIONER OF INCOME-TAX, MADRAS v. SIDDHA GOWDER AND SONS.

BEASLEY C.J.

family and carry on a money-lending business at Ootacamund. Up to the 24th May 1929 they also owned a half-share in a firm styled "K.G.S. & Co.", and a two-fifths share in a firm styled "B.K.S. & Co." doing other classes of business in Ootacamund. These two firms were dissolved on the 24th May 1929, an account was taken of their assets and liabilities, and those assets and liabilities, when ascertained, were distributed between the petitioners and another partner named B. K. Sunchai Gounder. The total of the liabilities falling to the share of the petitioner-family was Rs. 55,584. On this liability of Rs. 55,584, which represented borrowed money, a sum of Rs. 6,967 was due for interest at the time when the two businesses were dissolved and none of this interest had been paid. What the petitioners here seek to do is to deduct that sum of Rs. 6,967 from the profits made by them in their joint family money-lending business. The following facts have been found by the Income-tax Commissioner—and indeed they were admitted by the petitioners—viz., (1) that the deduction claimed represents the interest on capital borrowed entirely for the purpose of the two partnership businesses, viz., "K.G.S. & Co." and "B.K.S. & Co.", in which the petitioner family had a share, (2) that the said borrowed capital was raised by the two firms (by one of the two partners or by both of them jointly, acting on behalf of the two firms) from third parties and not from any of the petitioners' businesses, (3) that such borrowed capital was actually utilized in the two partnership businesses and (4) that on the dissolution of the two firms on 24th May 1929 the petitioner-family took over the liabilities of the two firms to the extent of Rs. 55,584 and paid Rs. 6,967 as interest thereon during the year of account. Upon those admitted facts the Income-tax Commissioner was of the opinion that the sum of Rs. 6,967 was not an amount

which could be deducted from the profits made by the petitioner joint trading family in Ootacamund in respect of the money-lending business. The argument put forward by Mr. S. Doraiswami Ayyar proceeded to a great extent to the consideration of the question as to whether, when an assessee is carrying on more businesses than one and in respect of one of them he has to borrow capital and pay interest thereon and in respect of that business in the year of account a loss results, such interest paid in respect of that borrowed capital can or cannot be set off against the profits made by the assessee in some other business. We were referred to decisions of this Court in support of that argument. It was not contended by Mr. Doraiswami Ayyar that any such deduction, which, of course, would be one under section 10 (2) (iii) of the Indian Income-tax Act, could be made directly from the profits and gains of the other business; but his contention was that, in respect of the business in which the capital was borrowed and interest upon which was paid and sought to be deducted in the ascertainment of the profits or gains of that business, obviously the deduction allowed under section 10 (2) (iii) could be made with a view to ascertaining whether that business had been carried on at a loss or profit. If it was discovered that the business was carried on at a loss, then it was contended that under section 24 of the Act that loss, so ascertained, could be set off against the profits and gains made in the other business. With that contention we entirely agree. It seems to be quite clear that, where more businesses than one are carried on, what has to be ascertained is whether they have resulted in a profit or whether one or some of them have resulted in a profit and others in a loss. If it is discovered that there has been a loss in one or more of them, that loss can, in our opinion, be set off under section 24 of the

COMMISSIONER OF INCOME-TAX, MADRAS v. SIDDHA GOWDER AND SONS.

BEASLEY C.J.

Act against the profits and gains of the other businesses of whatever description, and this view we take despite that taken by a Bench of this High Court consisting of SCHWABE C.J. and WALLER J. in *Commissioner of Income-tax* v. *Arunachelam Chettiar*(1). In that case it was held that where a person carries on two different trades, one individually and the other as a member of an unregistered firm, he is under section 10 (2) of the Income-tax Act, XI of 1922, entitled to set off, for purposes of income-tax, the loss incurred by him in respect of the partnership trade against the profit made by him in his individual trade. The view taken in that case by SCHWABE C.J. was that the loss made in the one trade could not be set off against the profit made in the other under section 24, because in his view that only enabled a loss in one class of business to be set off against the loss in another class of business. That, we think, is an incorrect view to take of that section; and the later decision of this High Court in *Commissioner of Income-tax, Madras* v. *Suppan Chettiar*(2), which takes the view that loss in one kind of business can be set off against a profit in a similar or other kind of business, is in our opinion correct upon that point. But in *Commissioner of Income-tax* v. *Arunachelam Chettiar*(1), holding the view that section 24 of the Act did not apply, the Bench then held that under section 10 the assessee was entitled to set off his loss in respect of one business against his gains in respect of the other taking the view that the words "profits or gains of *any* business carried on by him" mean "profits or gains of each and every business" carried on by him. It is not necessary for the purposes of this case to say more than that we doubt the correctness of that construction. The view

(1) (1923) I.L.R. 47 Mad. 660 (S.B.). (2) (1929) I.L.R. 53 Mad. 702 (S.B.).

we take is that the loss in one business after having been ascertained under section 10 can be set off under section 24 against the profits and gains in another business. That, however, does not conclude the matter because it is argued by Mr. Patanjali Sastri that we are not here considering any question of profits and gains made by the dissolved business in the year of account but what we are considering is a distribution of capital. It is pointed out that what happened when these two businesses were dissolved was a distribution of the assets and liabilities of these two businesses and that some assets fell to the share of the petitioner-family and also some of the liabilities, the liabilities in respect of which interest amounting to Rs. 6,967 had to be paid and in respect of which this deduction is claimed in this case. The argument on behalf of the assessees has proceeded on the footing that this is to be dealt with as a trading loss and that, if it is to be considered as a trading loss, the interest can be deducted from the profits, if any, of these businesses under section 10 (2) (iii), and the loss resulting from such deductions can then be deducted from the profits made by the undivided family ; but it seems to me to be quite clear that we are here dealing with capital loss as opposed to trading loss. Section 24 speaks of loss of profits or gains ; that means trading loss. This was not a trading loss in any sense. In this case the property of these two businesses was distributed after their dissolution ; and it was capital ; and authority for this view is to be found in the case of *Inland Revenue Commissioners* v. *Burrell*(1). There on the winding-up of a limited Company the undivided profits of past years and of the year in which the winding-up occurred were distributed among the share-holders of whom the respondent was one and it was held that

(1) [1924] 2 K.B. 52.

COMMISSIONER OF INCOME-TAX, MADRAS v. SIDDHA GOUDER AND SONS.

BEASLEY C.J.

super-tax was not payable on the undivided profits as income, because in the winding-up they had ceased to be profits and were assets only. Several cases are referred to in the course of the judgment of POLLOCK M.R. Amongst them is *In re Armitage. Armitage* v. *Garnett*(1), where LINDLEY L.J. observed as follows (page 346):—

> "The moment the company got into liquidation there was an end of all power of declaring dividends and of equalising dividends, and the only thing that the liquidator had to do was to turn the assets into money, and divide the money among the share-holders in proportion to their shares.";

and another case is *In re Crichton's Oil Company*(2), where STIRLING L.J. held that, upon a voluntary liquidation, a surplus of trading profit made in a particular year was distributable rateably among all the share-holders, as capital, and was not to be devoted as profits in the payment of a cumulative preferential dividend. These cases are of assistance to us in this case. It seems to me that what really was done in this case was to make a distribution of the property of the two businesses and that it was not open to the assessees to say upon such a distribution that some part of it represented trading profits and some part of it trading losses. It was in fact capital and, had there been any profit to the assessees on that distribution, it could not have been, it is conceded by Mr. Patanjali Sastri, liable to payment of income-tax. It follows, therefore, that where the distribution results in a loss no deduction in respect of that loss, such as is claimed here, can be claimed by the assessees. Under these circumstances, the answer to the question referred to us must be in the negative. Costs Rs. 250 to the Commissioner of Income-tax.

RAMESAM J.—I agree.

CORNISH J.—I agree.

A.S.V.

(1) [1893] 3 Ch. 337. (2) [1902] 2 Ch. 86.

SPECIAL BENCH.

Before Sir Owen Beasley Kt., *Chief Justice,*
Mr. Justice Ramesam and Mr. Justice Cornish.

THE COMMISSIONER OF INCOME-TAX, MADRAS, PETITIONER,

1931, December 16.

v.

A. RM. A. L. A. ARUNACHALAM CHETTIAR, RASIPURAM, SALEM DISTRICT, RESPONDENT.*

Indian Income-tax Act (XI of 1922), sec. 22 (3)—False return deliberately and dishonestly made—Penalty under sec. 28 for—Liability for—Revised correct return made by assessee and treated as revised return for purposes of sec. 22 (3)—Effect.

Section 22 (3) of the Indian Income-tax Act of 1922, which entitles an assessee to furnish a revised return, applies to a case in which he makes a *bona fide* discovery that he has made a previous incorrect return but not to a case in which the previous return was deliberately and dishonestly made.

Where an assessee made a return of his income deliberately and fraudulently omitting therefrom a large sum of money, and, on the point of the Income-tax Officer discovering that omission, the assessee put in a revised return including that sum, *held* that, although the later return might for the purposes of assessability to income-tax be treated as a revised return under section 22 (3), the Income-tax authorities were entitled to look at the previous incorrect return and were under section 28 of the Act entitled to inflict a penalty on the assessee.

REFERENCE to the High Court under section 66 (2) of the Indian Income-tax Act (XI of 1922) in thematter of Arunachalam Chettiar, Salem District.

R. Kesava Ayyangar for assessee.

M. Patanjali Sastri for Commissioner of Income-tax.

* Original Petition No. 148 of 1930.

COMMISSIONER OF INCOME-TAX, MADRAS v. ARUNACHALAM CHETTIAR.

BEASLEY C.J.

JUDGMENT.

BEASLEY C.J.—The Commissioner of Income-tax has of his own motion referred to us the following question :—

"Whether on the facts of this case the return submitted on the 7th January 1929 should have been treated as a revised return covered by the provisions of section 22 (3) of the Income-tax Act."

The assessee made a return of his income on the 22nd August 1928. Unfortunately that return was incorrect, not with regard to a small amount but to the extent of Rs. 34, 327. The Income-tax Officer has found, and his finding has been upheld by the Assistant Commissioner and the Commissioner of Income-tax, that the omission of that sum was deliberate. We take that to mean that the assessee knew when he made his return that it was false. After the assessee had made that return, the Income-tax Officer, whilst examining some other accounts, made certain discoveries and in the beginning of January 1929 he appeared to be on the point of discovering this deliberate and fraudulent omission of the assessee. Faced with this impending discovery, the assessee put in a revised return on the 7th January 1929 under section 22 (3) of the Indian Income-tax Act which reads as follows :—

"If any person has not furnished a return within the time allowed by or under sub-section (1) or sub-section (2) or having furnished a return under either of those sub-sections, discovers any omission or wrong statement therein, he may furnish a return or a revised return as the case may be at any time before the assessment is made, and any return so made shall be deemed to be a return made in due time under this section."

The Income-tax Officer assessed the assessee to income-tax on his revised return and at the same time inflicted on him a penalty of Rs. 2,000 under section 28

of the Act on account of the concealment of income. It is argued here that the assessee discovered on the 7th January 1929 that his previous return was an inaccurate one and that he was, therefore, entitled to claim the benefit of section 22 (3) and make a revised return and as that has been accepted no penalty can be inflicted upon him for having concealed his income. That certainly is a correct statement of what an assessee is entitled to claim, if he makes a *bona fide* discovery that he has made a previous incorrect return, but it certainly does not apply to the facts of this case which show clearly that the previous return was deliberately and dishonestly made. It is seriously argued that, notwithstanding that fact, the assessee is still enabled to put in a return correcting his former inaccurate one and that he is to be absolved from liability to have any penalty inflicted upon him. That, it seems to me, is to put a premium on dishonesty and nowhere in the Income-tax Act do we find any provision which does anything of the kind. The contention that this was a discovery within the meaning of section 22 (3) is of course futile. As the Income-tax Commissioner points out in his order of reference, the assessee did not discover on that day that he had made an incorrect return because at the time when he made his previous return he knew it was incorrect and he could not at any subsequent time have discovered something which he knew at an earlier time. Under these circumstances, the Income-tax authorities were perfectly correct and within their rights in inflicting the penalty upon the assessee. The answer to this question must, therefore, be that, although the later return may for the purposes of assessability to income-tax be treated as a revised return under section 22 (3), the Income-tax authorities are entitled to look at the previous incorrect return and are under section 28

COMMISSIONER OF INCOME-TAX, MADRAS v. ARUNACHALAM CHETTIAR.

entitled to inflict a penalty upon the person who has made it. Costs to the Commissioner Rs. 250.

RAMESAM J.—I agree.

CORNISH J.—I agree.

A.S.V.

SPECIAL BENCH.

Before Sir Owen Beasley Kt., *Chief Justice,*
Mr. Justice Ramesam and Mr. Justice Cornish.

1931, December 16.

THE COMMISSIONER OF INCOME-TAX, MADRAS, PETITIONER,

v.

RAJAH INUGANTI RAJAGOPALA VENKATA NARASIMHA RAYANIM BAHADUR VARU (ZAMINDAR OF KIRLAMPUDI A 2, ETC., ESTATES), RESPONDENT.*

Indian Income-tax Act (XI of 1922), sec. (2) (1) (a)—Agricultural income—Rent arrears and interest due by ryot to landholder—Promissory note taken from ryot by landholder for—Interest accrued due under—Agricultural income, if.

Interest due to a Zamindar under promissory notes taken by him from his ryots for the amount of rent due by them with interest is not "agricultural income" within the meaning of section 2 (1) (*a*) of the Indian Income-tax Act of 1922.

Sections 61 and 187 (2) of the Madras Estates Land Act only apply if a suit is brought directly on the liability of the ryot to pay rent. They are inapplicable to a case in which by a fresh contract between the Zamindar and the ryots the actual character of the liability has been changed into a loan.

REFERENCE to the High Court under section 66 (2) of the Indian Income-tax Act (XI of 1922) in the matter of the Zamindar of Kirlampudi.

P. V. Rajamannar for assessee.

M. Patanjali Sastri for Commissioner of Income-tax.

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* Original Petition No. 112 of 1930.