PRIVY COUNCIL.

THE COMMISSIONER OF INCOME-TAX, MADRAS, APPELLANT,

v.

P. R. A. L. MUTHUKARUPPAN CHETTIAR, RESPONDENT.

J.C.* 1935, May 24.

[ON APPEAL FROM THE HIGH COURT AT MADRAS.]

Indian Income-tax Act (XI of 1922), sec. 4 (2)—Partnership—Profits on dissolution—Assessment on profits.

On the dissolution of a partnership business in Ceylon, a portion of the capital of one of the partners resident in British India, and his share of the profits, were remitted to and received by him in British India.

Held, that the profits received in British India were assessable under section 4 (2) of the Indian Income-tax Act (XI of 1922).

Inland Revenue Commissioners v. *Burrell*, [1924] 2 K.B. 52, discussed. *Commissioner of Income-tax, Madras* v. *Siddha Gowder and Sons*, (1932) I.L.R. 55 Mad. 818 (S.B.), referred to.

APPEAL (No. 5 of 1935) from an order of the High Court (April 27, 1934) upon a reference by the Commissioner of Income-tax (November 19, 1932).

The facts of the case are stated in the judgment of the Judicial Committee.

DeGruyther K.C. and *Pringle* for appellant.—Profits received in British India by a partner on the dissolution of a partnership are assessable as profits of a business under sec. 4 (2) of the Indian Income-tax Act. The observation in *Commissioner of Income-tax, Madras* v. *Siddha Gowder and Sons*(1) to the contrary is erroneous. *Inland Revenue Commissioners* v. *Burrell*(2), relied on in that case, is a case relating to the winding-up of a company. The rule that the assets of a

* *Present:* Lord ATKIN, Sir JOHN WALLIS and Sir SHADI LAL.

(1) (1932) I.L.R. 55 Mad. 818 (S.B.).

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

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company distributed to shareholders on a winding-up is capital is inapplicable to a dissolution of a partnership. It is the property of the company that is distributed. There are no profits. In a dissolution of a partnership, the profits are ascertained before distribution and remain profits thereafter.

Chinna Durai and *Miss Miles* for the respondent referred to *Suleman* v. *Abdul Latif*(1) and the admission of Counsel for the Commissioner of Income-tax in *Commissioner of Income-tax, Madras* v. *Siddha Gowder and Sons*(2).

Appellant was not called on to reply.

LORD ATKIN.

The JUDGMENT of their Lordships was delivered by LORD ATKIN.—This is an appeal from the High Court at Madras on a reference under section 66 of the Indian Income-tax Act, 1922. The question is whether a sum of Rs. 38,305 was a receipt of capital or a receipt of profit assessable under section 4 (2) of the Income-tax Act. The facts are simple. The respondent is a Chetti carrying on business in Madras where he resides and in various other places within and without British India. He was up to May 1930 one of three partners in a money-lending business, S.P.K.A.A.M., at Colombo in which he had a six and three-fourths share. On 31st May 1930, he severed his connection with that firm, and an account was taken of the amounts due to him by way of capital, surplus capital, share of profit and interest thereon : and a sum of Rs. 2,09,670 was found due to him which included Rs. 23,500, share of profits from 26th October 1926 to 31st May 1930, and Rs. 38,305 interest on capital. The Rs. 23,500 was paid to him by hundis drawn by the remaining partners and cashed at Colombo. The Rs. 88,305 together with the greater part of the capital sum due was remitted to him in Madras

(1) (1930) I.L.R. 58 Calc. 208 ; L.R. 57 I.A. 245.
(2) (1932) I.L.R. 55 Mad. 818 (S.B.).

by the promissory note of a debtor of the firm made out in the respondent's favour. No question of fact arises on the reference which can only raise a question of law. The only question for the Court is whether the sum of Rs. 38,305 received by the respondent in Madras in respect of interest on capital employed in business in Ceylon is assessable under section 4 (2) of the Income-tax Act. No dispute arises as to the sum being derived from business : the only question is whether the effect of the dissolution was to make payment of all the sums due on dissolution payments by way of capital and not payments of income or profits. The High Court, following a decision of their own in *Commissioner of Income-tax, Madras* v. *Siddha Gowder and Sons*(1), held that the principles laid down in the English case of *Inland Revenue Commissioners* v. *Burrell*(2) governed the case and decided in favour of the respondent. But that case involved what appears to their Lordships quite a different set of facts, the receipt by a shareholder of his share of the assets of a company upon a winding-up. It was pointed out in the judgments of the Court of Appeal that a company is a separate entity to the shareholders ; that during the continuance of the company the latter have no right to the profits except so far as they are distributed on a regular declaration of dividend ; and that on winding-up their sole right is to share in the assets available after winding-up ; and that for the purpose of ascertaining such assets it is quite immaterial whether the company originally

(1) (1932) I.L.R. 55 Mad. 818 (S.B.). (2) [1924] 2 K.B. 52.

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possessed them by way of capital or profits. The liquidator may apply sums earned as profits in paying capital liabilities and capital assets in paying revenue liabilities. What he distributes is a lump sum, and no reconstruction into a division of capital and profits is necessary or in many cases possible. The position in respect of a partnership is different. The profits are the profits of the partners, joint in the first instance, and if the appropriate statute so provides assessable as joint ; but in fact representing an interest of each partner, and as soon as declared constituting an obligation from the firm to each partner. If the Ceylon Ordinance be analogous to the English Act there would be no doubt that up to May 1930 the respondent would have been assessable to income-tax jointly and to surtax severally on the amount of the profits in question. And if in fact, instead of being left in Colombo undrawn, the sums in question had before May 1930 been remitted to the respondent in India no question would have arisen as to his having been assessable under the Indian Act on those sums. Being profits of the respondent up to 31st May 1930 how did they alter their character by dissolution ? The account taken on dissolution ascertains what is due to the partners for profits, and what is due for capital. It can hardly be suggested that the partners share according to their capital proportions in the whole assets of the partnership. The sum due for undrawn profits was and remains a sum due by the partners to each partner, and necessarily ranks first before the sums due for capital can be distributed. In other

words, on dissolution of a partnership an outgoing partner has the right to receive not, as in the case of a shareholder in winding-up a company only a share of the assets, but to receive payment of his profits, profits which were his before dissolution and do not cease to be his on dissolution. In their Lordships' opinion the respondent received this payment in India as a payment of profits and was properly assessed. Counsel for the respondent pointed out that the contention of the Commissioner in this case was the contrary of that made by him in the previous case in Madras which was successful in the High Court. He protested strongly against the Commissioner in successive cases blowing hot and cold. But that is a privilege not confined to Commissioners of Income-tax and its exercise cannot influence judicial determination of the law. Their Lordships think it desirable to point out that their decision does not cover cases where undrawn profits have with the consent of all parties been invested in the business so as to increase the capital account, a position which does not arise here. Nor have they had to consider any special provisions of partnership articles which might affect the matter, for there were none in this case. For the reasons given they are of opinion that this appeal should be allowed, the order of the High Court dated 27th April 1934 should be set aside and the question referred to the Court by the Commissioner should be answered that the sum of Rs. 38,305 is receipt of profits assessable under section 4 (2) of the Income-tax Act. The respondent must pay the costs here and in the High Court.

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Their Lordships will so humbly advise His Majesty.

Solicitor for appellant: *Solicitor, India Office.*

Solicitors for respondent: *Douglas Grant & Dold.*

A. M.T.

APPELLATE CIVIL—FULL BENCH.

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

1934, December 21.

1935, February 20.

T. R. B. RANGANATHA REDDI (PLAINTIFF), APPELLANT,

v.

RAMASWAMI MUDALI AND SIX OTHERS (DEFENDANTS TWO AND FOUR AND TWENTY TO TWENTY-FOUR), RESPONDENTS.*

Indian Limitation Act (IX of 1908), sec. 6—Child en ventre sa mere—Applicability of section to.

A Hindu father alienated the joint family properties at a time when his son was a child *en ventre sa mere.* The son filed a suit to set aside the alienations on the day before the three years' period of limitation from the date of his attaining majority had expired. A question arose as to whether the plaintiff could take advantage of section 6 of the Indian Limitation Act.

Held, that section 6 of the Indian Limitation Act was applicable and that the suit was not barred by limitation.

Muhammad Khan v. *Ahmad Khan,* (1928) I.L.R. 10 Lah. 713, dissented from.

APPEAL against the decree of the Court of the Subordinate Judge of Vellore in Original Suit No. 65 of 1924.

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* Appeal No. 30 of 1932.