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that the decree finally determined the right of the parties, and is therefore a "judgment" within the meaning of clause 13 of the Letters Patent.

The only remaining question is whether at the hearing of an appeal from the decree of the 11th of July 1934 it is open to the appellant to canvass the validity of the order of the 3rd of July 1934 upon which the decree is based. I am disposed to think that the appellant is at liberty to do so [section 105 of the Code of Civil Procedure and *Madanlal Lachmandas* v. *Kedarnath Shersinghdas* (1)]. On the merits there is no substance in the appeal.

For these reasons, in my opinion, the appeal fails and must be dismissed with costs.

MYA BU, J.—I agree.

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## INCOME-TAX REFERENCE.

*Before Sir Arthur Page, Kt., Chief Justice, Mr. Justice Mosely, and Mr. Justice Ba U.*

1935

*Jan. 28.*

## *IN RE* THE COMMISSIONER OF INCOME-TAX, BURMA

*v.*

## M.A.L. CHETTIAR FIRM.*

*Income-tax—Chettiar money-lenders—Mercantile system of accounting—Interest added to principal amount—Fresh promissory note for principal and interest—Interest as income.*

The chettiar money-lenders in Rangoon generally adopt the mercantile system of accounting in transactions with their non-chettiar customers. On the acceptance of a new promissory note the creditors treat the interest which forms part of the capital loan under the new promissory note as having been received by the creditors from their debtors. In effect, they give up the right to recover the loan and interest under the old transaction in consideration of the obligations undertaken by the debtors under the new promissory note representing the interest due under the old loan which is capitalized for the purposes of the new transaction. They invest the old interest as capital in the new loan.

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(1) 32 Bom. L R. 660 at p. 663.

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*Held*, that under the circumstances the Income-tax Officer had material to treat such interest as income liable to income-tax.

*The Commissioner of Income-tax, Burma* v. *V.S.A.R. Firm*, I.L.R. 13 Rang. 231 —*followed*.

*Secretary to the Board of Revenue, Income-tax, Madras* v. *M.Ar.Rm. Arunachalam Chettyar*, I.L.R. 44 Mad. 65—*referred to*.

*N. M. Cowasjee* for the assessees. To give security for a debt is not to pay the debt. A debtor who gives a promissory note for the sum he owes can in no sense be said to pay his creditor; he merely gives him a document possessing certain legal attributes. Moreover, the execution of a promissory note by a debtor in favour of his creditor is only conditional payment of the debt. *Raja Raghunandan Prasad* v. *Commissioner of Income-tax, Bihar and Orissa* (1); *Commissioner of Income-tax, Bihar and Orissa* v. *Maharajadhiraj of Darbhanga* (2). The assessees have had to enter the interest in question in their books of account as having been received because the accounts had to be balanced somehow.

[PAGE, C.J. Where the assessee chooses to treat a sum of money as having been received, can it be said that there are no materials before the income-tax authorities to justify a finding that the sum is taxable? In *Raja Raghunandan Prasad*'s case the interest was not shown as realized in the books of account of the assessee.]

But what was the evidence before the income-tax authorities in the present case; only the promissory notes and the entries in the books of account? On these materials the income-tax authorities have chosen to disbelieve the statement of the assessees that they have not, in fact, received the interest sought to be taxed. The question in this case has not been

(1) I.L.R. 12 Pat. 305, 311. (2) I.L.R. 12 Pat. 318, 336.

properly framed. The real question is whether the assessees have received the interest stated in their books of account as having been received. In such cases the Court has power to reframe the question and decide it.

[PAGE, C.J. The Court has no power to do so. See *In re The Commissioner of Income-tax, Burma* v. *C.P.L.L. Firm* (1).]

Interest which merely accrues due, but is not received in the year of assessment cannot be taxed in that year. *Secretary to the Board of Revenue* v. *Al.Ar.Rm. Arunachalam Chettyar* (2).

[PAGE, C.J. But see Napier J's observations on p. 74 where he points out that a creditor entitled to receive interest may agree to leave such interest in the hands of his debtor either by way of deposit or as a fresh loan, and such interest would be taxable.]

Sadasiva Ayyar J. sets out the true position on p. 80. Entries in the books of account are in no way conclusive [*Doughty* v. *Commissioner of Taxes* (3)]. If the interest has become so completely under the control of the assessee that by an act of his will he could receive it in cash without greater trouble than is involved in drawing money from his banker then it will be taxable.

*A. Eggar* (Government Advocate) for the Crown. *Secretary to the Board of Revenue* v. *Arunachalam Chettyar* was a decision under the old Act of 1918, and the learned Judges were trying to show that an

(1) I.L.R. 12 Ran. 322. (2) I.L.R. 44 Mad. 65.
(3) (1927) A.C. 327.

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income may be constructively received. The Legislature has in 1922 expanded the word "income" into "income, profits and gains" and has added s. 13. There is no magic in the method of accounting adopted. The sole question in each case is, how is the taxable income to be estimated, and how has the assessee estimated it? The assessees here have entered the interest as having been received, and have further loaned it out as fresh capital earning further interest. The present case is covered by the decision in *Commissioner of Income-tax, Burma* v. *V.S.A.R. Firm* (1). Moreover, if the interest was not taxed the assessee may contend in a later year when the assessment falls to be made that the sum in question is principal and not taxable, and only the interest actually received in that year should be taxed.

PAGE, C.J.—In this case the question propounded is :

"Whether there was evidence on which the Income-tax Officer could conclude that the assessees' method of accounting was the mercantile or accrued method in respect of the sum of Rs. 57,518, interest from non-chettyar debtors shown in the assessees' accounts and taxed in the assessment."

In my opinion this case is governed by the decision of this Court in *The Commissioner of Income-tax Burma* v. *V.S.A.R. Firm, Rangoon* (1). The only difference in the facts between the two cases is that, whereas in *The Commissioner of Income-tax, Burma* v. *V.S.A.R. Firm, Rangoon* (1) the new promissory note related both to the principal and to the interest that had accrued upon it, the new promissory note in the present case refers to the interest only.

(1) (1935) I.L.R. 13 Ran. 231.

In my opinion the same principle governs the two cases. As was pointed out in *The Commissioner of Income-tax, Burma* v. *V.S.A.R. Firm, Rangoon* (1), the real question that falls for determination is :

"Whether there were materials before the Income-tax Officer upon which he could find that the sum of Rs. 57,518 was interest upon loans that had accrued to the assessees in the accounting year, and as such was assessable to income-tax for the year 1933-34."

We have heard an elaborate argument on behalf of the assessees the burden of which was that the Income-tax Officer had arrived at a wrong conclusion upon the materials before him. It is necessary to emphasize once more that the question is not whether the conclusion at which the income-tax authorities arrived was correct, but whether there was material before the income-tax authorities upon which they could have arrived at the conclusion which they reached. There is little to add to the judgment in *The Commissioner of Income-tax, Burma* v. *V.S.A.R. Firm, Rangoon* (1). It is not uninstructive, however, to notice how the matter was put in a case to which the learned advocate for the assessees referred [*The Secretary to the Board of Revenue, Income-tax, Madras* v. *Al.Ar.Rm. Arunachalam Chettyar and Brothers* (2)]. In that case a Special Bench of the Madras High Court was dealing with a case stated under section 51 of the Income-tax Act (VII of 1918) and, as Wallis C.J. pointed out, the only question that was argued in that case was "whether money which became due to a money-lending firm in the course of its business by way of interest in the year of account, or year on the income of which

(1) (1935) I.L.R. 13 Ran. 231. (2) (1920) I.L.R. 44 Mad. 65.

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the tax is to be assessed for the current year, is to be treated as part of the assessable income for that year of account, although it was not recovered or realized by the firm in that year, either in cash or by adjustment in the accounts." And in the course of his judgment Napier J. (at page 92) expressed the opinion that

"if a person entitled to receive money agrees with his debtor to let the money stand in the hands of the debtor, either by way of deposit *or as a fresh loan or investment*, that would, in my opinion, amount to receipt."

In the present case in the course of the argument I asked the learned advocate for the assessees what his defence would be if after a fresh promissory note had been executed a suit had been brought against the debtors to recover the interest due under the old loan, and his answer inevitably was that the old loan had been discharged by the acceptance of the new promissory note. As was pointed out in *The Commissioner of Income-tax, Burma* v. *V.S.A.R. Firm, Rangoon* (1), in *Raja Raghunandan Prasad Singh* v. *Commissioner of Income-tax, Bihar and Orissa* (2) Lord Macmillan had observed

"that the sum of Rs. 2,33,135 was 'not shown separately as interest realized in the assessees' books of account of that year (*i.e.* 1904) either in the interest account or in the personal account of the debtor'—a finding which seriously stultifies the question as framed by the Commissioner."

Now, in the present case as in *The Commissioner of Income-tax, Burma* v. *V.S.A.R. Firm, Rangoon* (1) both in the interest account of the assessees and in the account which they kept relating to the debts of their respective debtors the interest in question is

(1) (1935) I.L.R. 13 Ran. 231. (2) (1933) I.L.R. 12 Pat. 305.

shown as having been received by the assessees during the year of account, and it is so stated in the profit and loss account of the firm.

The learned advocate for the assessees contended that it was inevitable that this sum, representing the interest under the old loan, should have been entered as "received" in the interest account and the debtors' account kept by the assessees. He stated that the assessees "must give credit for the interest in their accounts"; but that is not so. Where accounts as between the assessees and other chettyar firms are concerned no doubt according to the system of accounting adopted by the assessees interest accrued during the accounting year is entered in the accounts as interest for which the assessees took credit as having been received during the accounting year, and as they have adopted that method of accounting in respect of other chettyar firms no complaint is raised to the effect that notional receipts of interest should not be treated for purposes of income-tax as upon the same footing as actual receipts. The mercantile system probably works out as satisfactorily to the assessees and the income-tax authorities as does the method of accounting known as the cash system. But it so happens that in connection with their transactions with non-chettyars the assessees normally adopt the cash system, and if in connection with a transaction such as those under consideration in which a fresh loan is taken for debts already accrued from non-chettyars the cash system of accounting had been adopted, so far from there being any necessity for an entry in their book of accounts that the assessees had "received" the interest, which had accrued but not been actually received, such an entry would be contrary to the form of accounting that they had adopted. It appears,

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however, that in transactions with non-chettyars in which a fresh loan is taken for an accrued debt the assessees,—indeed, the chettyar community in general,—adopt the mercantile system of accounting, and on the acceptance of a new promissory note treat the interest which forms part of the capital loan under the new promissory note as having been received by the assessees from their debtors. In effect what happens is that the assessees are content to stay their hand in connection with the recovery of the loan and interest under the old transaction in consideration of the obligations undertaken by the debtors under the new promissory note which consists of the interest due under the old loan which is capitalized for the purposes of the new transaction. In other words, as the learned Government Advocate pointed out, the assessees were investing the old interest as capital in the new loan. In such circumstances it appears to me that there was material before the Income-tax Officer upon which he could come to the conclusion that the sum of Rs. 57,518 was interest upon loans that had accrued to the assessees in the accounting year, and as such was assessable to income-tax for the year 1933-34.

I would answer the question propounded in the affirmative. The learned Government Advocate is entitled to his costs, ten gold mohurs.

MOSELY, J.—I agree.

BA U, J.—I agree.