

1927. The appellant's costs in this Court and in the Court of the District Judge should be paid by the respondent.

DIN MOHAMMAD J.—I agree.

A. N. C.

Appeal accepted.

1934

MUSSAMMAT
MEL KAUR

v.

DAULAT RAM.

HILTON J.

CIVIL REFERENCE.

Before Addison and Sale JJ.

KANGRA VALLEY SLATE COMPANY, LTD.

(ASSESSEE) Petitioner

versus

COMMISSIONER OF INCOME-TAX, PUNJAB—

Respondent.

1934

June 28.

Civil Reference No. 25 of 1932.

Indian Income-tax Act, XI of 1922, Section 10 (2) (ix): Expenses incurred in defending a law suit—whether deductible—difference between 'Capital' and 'Income' expenditure—pointed out.

The question referred to the High Court by the Commissioner of Income-tax was whether the expenditure incurred by the assessee-company in defending, as lessees of certain land, a suit for ejection and injunction instituted by the lessors, is deductible under Section 10 (2) (ix) of the Income-tax Act as expenditure "incurred solely for the purpose of earning such profits or gains."

Held, that the answer to the reference depends on the question whether the legal expenditure incurred by the Company was or was not in the nature of capital expenditure.

And, applying the test laid down by Lord Dunedin in *Vallambrosa Rubber Co. Ltd. v. Farmer (Surveyor of taxes)* (1), *viz.* "that capital expenditure is a thing to be spent once and for all, and income expenditure is a thing that is

1934
 —
 KANGRA
 VALLEY SLATE
 COMPANY, LTD.
 v.
 COMMISSIONER
 OF
 INCOME-TAX.

going to recur every year," that the expenditure in the present case is in the nature of capital expenditure and that the answer to the reference must, therefore, be in the negative.

Small v. Easson (Surveyor of taxes) (1), and *Marant (Surveyor of taxes) v. Wheal Grenville Mining Co.* (2), relied upon.

Usher's Wiltshire Brewery, Ltd. v. Bruce (Surveyor of taxes) (3), distinguished.

Case referred under Section 66 (3) of the Income-tax Act by Mr. W. R. Pearce, Commissioner of Income-tax, Punjab, Lahore, with his No. 221-10/33-1046, dated 18th November, 1933, for orders of the High Court.

BADRI DAS, for Petitioner.

J. N. AGGARWAL, for Respondent.

The judgment of the Court was delivered by—

SALE J.—The Commissioner of Income-tax has referred to us for our opinion the question whether the expenditure incurred by the Kangra Valley Slate Company, Limited, in defending as lessees of certain land in *Mauza Kanhyara*, District Kangra, a suit for possession and injunction instituted by the lessors, who are the proprietary body of that village, is deductible under clause (ix), sub-section (2) of section 10 of the Income-tax Act.

The material facts of this case are that the Kangra Valley Slate Company, Limited, by lease, dated the 22nd February, 1867, secured in perpetuity the exclusive right of quarrying slate in Kanhyara village of the Kangra District. The Company is also a share-holder in the village *shamilat* and as such enjoyed quarrying rights in common with the

(1) (1920) 12 Tax Cases 351. (2) (1894) 3 Tax Cases 298.

(3) (1914) 6 Tax Cases 399.

proprietary body; but the essence of the company's business is that by reason of the lease it enjoys a monopoly of slate quarrying in this village.

This monopoly has been recently assailed by the village proprietary body who, on the 10th July, 1928, instituted a suit to eject the company from the quarries covered by the lease and also for an injunction to prevent the company from quarrying. On 11th July, 1930, a decree was passed against the company by the trial Court and an appeal against that decree is pending in this Court. The company have obtained stay of execution so far as the injunction is concerned so that the business of the company continues during the pendency of the appeal. In submitting a return of its income for the year ending 30th June, 1930, which is the "previous year" for the purpose of assessment under consideration (1931-32), the company showed a net income of Rs. 23,350 which was arrived at after deducting Rs.13,397 on account of the legal expenses of the suit to date. The Income-tax Officer supported by the Commissioner, Income-tax, has held that no deduction is permissible because the legal expenses were expenditure in the nature of capital, and since it was not incurred solely for the purpose of earning the profits and gains of a business it did not fall within the purview of section 10 (2) (*ix*) of the Income-tax Act.

Paragraph (*ix*) of sub-section (2) of section 10 of the Income-tax Act provides that allowances may be made on—

"any expenditure (not being in the nature of capital expenditure) incurred solely for the purpose of earning such profits or gains."

1934

KANGRA
VALLEY SLATE
COMPANY, LTD.
v.
COMMISSIONER
OF
INCOME-TAX.

1934

KANGRA
VALLEY SLATE
COMPANY, LTD.
v.
COMMISSIONER
OF
INCOME-TAX.

Mr. Badri Das on behalf of the company urges that the cost of the litigation was incurred to defend the monopoly of quarrying which is the very life-blood of the company. For this reason he contends that the expenditure should be held to have been incurred solely for the purpose of earning profits or gains; since if the monopoly were lost, the business of the company would come to a stand-still, and there would be no profits or gains. Further he contends that the expenditure is debitable to revenue and is not capital expenditure, and that for these reasons the deduction is permissible under the clause. The opinion of the Commissioner is that since the subject matter of the suit represents the capital of the company, the expenditure on litigation was incurred to defend the capital of the business and must, therefore, be deemed to be in the nature of capital expenditure. Accordingly he holds that no deductions can be permitted.

No authority applicable to the facts of this case has been cited before us at the Bar. Counsel for the assessee has invited our attention to a British case *Usher's Wiltshire Brewery, Ltd. v. Bruce* (*Surveyor of taxes*) (1), in which a Brewery company, as lessees of a number of houses which they had acquired in the course of their business, claimed deductions on account of certain expenditure as being money wholly and exclusively laid out for the purpose of the Brewery; and this claim was upheld on appeal to the House of Lords. The only point of relevance in this case is that a sum of £66-2-8 was included in the expenses thus claimed and allowed as legal and other costs. This authority, however, has no bearing upon the present case, partly because this item

(1) (1914) 6 Tax Cases 399.

for legal expenses, being trifling in comparison which the other expenses claimed, passed practically unnoticed in the course of the legal discussion and also because (as would appear from page 410 of the ruling) it was agreed between counsel at the commencement that these legal expenses "were not incurred for any extension of the business so as to make them 'capital' expenses." In our opinion the answer to the reference made by the Income-tax Commissioner in the present case depends on the question whether the legal expenditure incurred by the Kangra Valley Slate Company was or was not in the nature of capital expenditure; and since it was agreed that the legal expenses permitted in Usher's case, *Usher's Wiltshire Brewery, Ltd. v. Bruce (Surveyor of taxes)* (1) were not to be considered capital expenditure, the authority has no bearing on the present dispute.

As observed by Wright J. in *Marant (Surveyor of taxes) v. Wheal Grenville Mining Co.* (2) the question whether certain expenditure in respect to which a deduction is sought is capital or not is in its essence one of fact; and as such it is open to question whether this is a permissible reference to us under section 66 of the Income-tax Act. But we have no doubt that this reference should be treated as involving a question of law. It should, however, be understood that in answering this reference we are not deciding any question of principle; but are giving our opinion which is relevant solely to the facts of the case before us.

The Income-tax Act does not contain any definition of the term 'capital expenditure' nor has any definition been attempted in the various authorities

1934

KANGRA
VALLEY SLATE
COMPANY, LTD.
v.
COMMISSIONER
OF
INCOME-TAX.

(1) (1914) 6 Tax Cases 399.

(2) (1894) 3 Tax Cases 298.

1934

KANGRA
VALLEY SLATE
COMPANY, LTD.
v.
COMMISSIONER
OF
INCOME-TAX.

cited at the Bar. The nearest approach to a definition of 'capital expenditure' occurs in certain observations by Lord Dunedin in the case of *Vallambrosa Rubber Co., Ltd. v. Farmer (Surveyor of taxes)* (1). Lord Dunedin observed (on page 536) as follows:—'I think it is not a bad criterion of what is capital expenditure as against what is income expenditure, to say that capital expenditure is a thing that is going to be spent once and for all and income expenditure is a thing that is going to recur every year.' This test laid down by Lord Dunedin was approved in the case reported as *Small v. Easson (Surveyor of taxes)* (2) in which the Lord Justice Clerk at page 355, observed that this criterion has been accepted in several subsequent cases.

The expenditure incurred by the Kangra Valley Slate Company, Limited, in the present case was clearly a non-recurring outlay required to retain a capital asset. Following the criterion laid down by Lord Dunedin in the *Vallambrosa case* (1) we hold that the expenditure incurred by the Kangra Valley Slate Company, Limited, in this particular case is in the nature of capital expenditure and we agree, therefore, with the Commissioner of Income-tax in answering the question referred to us in the negative.

A. N. C.

Reference answered in the negative.

(1) (1910) 5 Tax Cases 529, 536.

(2) (1920) 12 Tax Cases 351, 355.