

SUREME COURT OF INDIA

Commissioner of Income-Tax, Madhya Pradesh, Nagpur And Bhandara

Vs.

Kalooram Govindram

(J Shah, K S Rao and S Sikri JJ.)

22.03.1965

JUDGMENT

SHAH, J.

1. The respondent is a Hindu undivided family which carried on business among others in oil mills, sugar mills and ginning factories. The respondent formed an association with another Hindu undivided family - Ganga Prasad Bachhulal - to carry on a business styled "Govindram Sugar Mills." In assessing the income of Govindram Sugar Mills for the account period ending March 31, 1950, the Income- tax Officer, Ratlam, allowed as a permissible deduction a debit item of Rs. 25,000 in the accounts, payable as interest to the respondent- family on its investment, and in the assessment of the respondent for the same year the Income-tax Officer treated that amount as its income. In the relevant year of account Govindram Sugar Mills had incurred loss, and the loss being of an association of persons, the Income-tax Officer declined to allow the respondent's share of loss in its assessment, and rejected the contention of the respondent that no income had in fact been earned by the respondent. The Appellate Assistant Commissioner confirmed the order of the Income-tax Officer. But the Income-tax Appellate Tribunal allowed the appeal and deleted the interest on investment in the computation of the income of the respondent. The Tribunal observed that "The assessee s total profit from the mills... arises on account of the carrying on of the mills. Allowance of interest is only an appropriation of the same profits in order to adjust the rights of the various members inter se. Therefore... it is not correct for the department to include as an item of income and disallow the loss on the ground that it is a loss of an association of persons. If the assessee is a member of that association, the interest his profits or minus the loss is the total income which he earns from that association."

2. In considering the following question referred by the Tribunal :

Whether, on the facts and in the circumstance of the case, interest calculated on the advance made to Govindram Sugar Mill is assessable in the hands of the assessed ?"

3. The High Court of Madhya Pradesh held that the entries posted in the books of account of Govindram Sugar Mills were merely book entries and were not in conclusive of the question whether the respondent had become entitled to the sum. In the view of the High Court the credit

entry on account of interest in favour of the respondent for an amount less than the respondent's share of loss in the business must be regarded as a mere book entry and having regard to the substance of the matter, there was no real income in the shape of interest on the capital invested in the business". Against this order passed by the High Court, with certificate of fitness granted by the High Court, this appeal has been preferred.

4. In our view the High Court was right in holding that there was no real income received by the respondent. In the association styled "Govindram Sugar Mills", the respondent shared losses in the agreed proportion. Govindram Sugar Mill incurred heavy losses in its business transactions in the relevant year of account. Debit entries in the books of account of the association relating to interest deemed payable on investments were posted, but it could not as a matter of law be inferred therefrom that any part of the income of the association was distributed. The share of the respondent in the loss suffered by Govindram Sugar Mills was considerably in excess of the amount of interest debited as payable in the respondent's account with the association. Entries relating to interest payable to the two members of the association were posted merely for apportionment of part of the loss suffered by the sugar mills : they represented no real income to the two members. The Tribunal and the High Court were, therefore, right in regarding the entry as a mere book entry nor representing true income.

5. Counsel for the Commissioner urged that as the amount of interest was allowed as a permissible outgoing in the assessment of the association, a corresponding amount should be regarded as received by the respondent as income. But an error in the assessment of the association cannot be permitted to be perpetuated by repeating it in the assessment of the respondent. It is true that the interest debited to the profit and loss account of the association to the two members is not in proportion to their respective shares in the profit and loss account according to the terms of the agreement. But apportionment of loss suffered by the association, in proportion to the investments of the two members and not in proportion to their stipulated shares in profit and loss, does not convert the debit items into real income accruing to the two members.

6. The appeal fails and is dismissed with costs.

7. Appeal dismissed.