Commissioner of Income-Tax, Calcutta

Vs

Jaipuria China Clay Mines (P) Ltd

C.A. No. 307 of 1964

(K. Subha Rao, J. C. Shah, S. M. Sikri JJ)

01.11.1965

JUDGMENT

SIKRI, J. –

This is an appeal by certificate granted by the High Court of Calcutta its judgment in a reference made to it under s. 66 of the Indian Income Tax Act, 1922 (hereinafter referred to as the Act.) The question referred to it by the Appellate Tribunal, at instance of the assessee, was as follows :

> "Whether in the facts and circumstances of the case, the unabsorbed depreciation of the past years should be added to the depreciation of the current year and the aggregate of the unabsorbed depreciation and the current year's depreciation be deducted from the total income of the previous year relevant for the assessment year 1952-53."

The relevant facts and circumstances are as follows : The Income Tax Officer assessing the respondent, M/s Jaipuria China Clay Mines (p) Ltd. Calcutta, hereinafter referred to as the assessee, for the year 1952-53 computed its total income at Rs. 14,041/- before charging depreciation for that year. From that figure he deducted depreciation for the year amounting to Rs. 5.360/-, thus computing a profit of Rs. 8,681/-. From this figure he deducted an equivalent amount, i.e., Rs. 8,681/-, in respect of losses during 1947-48, and he thus worked out the business income as nil. He then computed the dividend income at Rs. 2,01,130/- and determined the total income at this figure and levied tax on it. The assessee had in its favour an unabsorbed depreciation aggregating to Rs. 76,857/-, and it contended before the Income Tax Officer that this sum should be deducted from the income received from dividends, which, if done, would reduce the total income to Rs. 1,32,955/-, but the Income Tax Officer refused to accede to this contention. The Appellant Assistant Commissioner upheld the order of the Income Tax officer and the assessee's appeal to the Appellate Tribunal met with the same fate. The High Court, however, accepted the contention of the assessee and answered the question referred to it in favour of the assessee.

The answer to the question depends on the interpretation of ss. 6, 10 and 24 of the Act. We are concerned with the law as it stood on April 1, 1952. The scheme of the Act is that the tax is levied in respect of the total income of the previous year of every individual, Hindu Undivided family, etc., and the total income consists of income under various heads such as Salaries, Interest on Securities, Income from Property, Profits and gains of business, profession or vocation, and Income from other sources and Capital gains. Various sections deal with how income, profits and gains under each head to be computed. Section 10 deals with the computation of profit and gains of any business carried on by an assessee. Section 10(2) prescribes the allowances which have to be deducted before

computing computing the profits and gains; one of the allowances is 'depreciation', and this is provided under sub-cl. (vi). Proviso (b) to s. 10(2)(vi). On this a great deal of argument has been addressed to us and it reads as follows :

> "(b) where, in the assessment of the assessee or if the assessee is a registered firm, in the assessment of its partners, full effect cannot be given to any such allowance in any year not being a year which ended prior to the 1st day of April, 1939, owing to there being no profits or gains chargeable for that year, or owing to the profits or gains chargeable being less than the allowance, then, subject to the provisions of clause (b) of the proviso to sub-section (2) of section 24, the allowance or part of the allowance to which effect has not been given, as the case may be, added to the amount of the allowance for depreciation for the following year and deemed to be part of that allowance, or if there is no such allowance for that year, he deemed to be the allowance for that year, and so on for succeeding years;"

It may be mentioned that the words "in the assessment of the assessee or if the assessee is a registered firm, in the assessment of its partners" were inserted by s. 8 of the Indian Income Tax (Amendment) Act, 1953 (25 of 1953) with effect from April 1, 1952. The next relevant statutory provision is s. 24, which provides for set off of losses in computing aggregate income. Relevant portions of s. 24 are in the following terms :

> "24(1) Where any assessee sustains a loss of profits or gains in any year under any of the heads mentioned in section 6, he shall be entitled to have the amount of the loss set off against his income, profits or gains under any other head in that year......

Provided that......

> Provided further that when the assessee is an unregistered firm which has not been assesses under the provisions of clause (b) of sub-section (5) of section 23, in the manner applicable to a registered firm, any such loss shall be set off only against the income, profits and gains of the firm and not against the income, profits and gains of any of the partners of the firm; and where the assessee is a registered firm, any loss which cannot be set off against other income, profits and gains of the firm shall be apportioned between the partners of the firm and they alone shall be entitled to have the amount of the loss set off under this section.
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> (2) Where any assessee sustains loss of profits or gains in any year, being a previous year not earlier than the previous year for the assessment for the year ending on the 31st day of March, 1940, in any business, profession or vocation and the loss cannot be wholly set off under sub-section (1), so much of the loss as is not so set off or the whole loss where the assessee had no other head of income, shall be carried forward to the following year and set off against the profits and gains, if any, of the assessee from the same business, profession or vocation for that year; and if it cannot be wholly so set off, the amount of loss not so set off shall be carried forward to the following year, and so on; but no loss shall be so carried forward for more than six years, and a loss arising in the previous years for the assessment for the years ending on the 31st day of March, 1940, the 31st day of March, 1941, the 31st day of March, 1942, the 31st day of March, 1943, and the 31st day of March, 1944, respectively, shall be carried forward only for one, two three, four and five years, respectively :

Provided that -

(a) ......

> (b) where depreciation allowance is, under clause (b) of the proviso to clause (vi) of sub-section (2) of section 10, also to be carried forward, effect shall first be given to the provisions of this sub-section;
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> (c) nothing herein contained shall entitle any assessee, being a registered firm, to have carried forward and set off any loss which has been apportioned between the partners, under the proviso to sub-section (1), or entitle any assessee, being a partner in an unregistered firm which has not been assessed under the provisions of clause (b) of sub-section (5) of section 23 in the manner applicable to a registered firm, to have carried forward and set off against his own income any loss sustained by the firm;...."

Mr. Sastri, learned counsel for the revenue, urges that depreciation, although a permissible allowance under s. 10(2) of the Act, serves to compensate an assessee for the capital loss suffered by him by way of depreciation of his assets. He says that if it had not been expressly allowed as allowance, it would have been treated as capital expenditure and would have been excluded. He further says that depreciation is a charge on the profits of a business. Bearing these two factors in mind, he urges that the expression "loss of profits and gains" in s. 24(1) does not include any deficiency resulting from depreciation and, therefore, an assessee is not entitled to ask the Department to include the depreciation in the amount which can be set off against income, profits and gains under other heads such as income from property or dividends. Mr. Rajgopala Sastri for the assessee relies on the history of the legislation and a number of authorities to support the judgment of the High Court.

Apart from authority, looking at the Act as it stood on April 1, 1952, it is clear that the underlying idea of the Act is to assess the total income of an assessee. Prima facie, it would be unfair to compute the total income of an assessee carrying on business without pooling the income from business with the income or loss under other heads. The second consideration which is relevant is that the Act draws no express distinction between the various allowances mentioned in s. 10(2). They all have to be deducted from the gross profits and gains of a business. According to commercial principles, depreciation would be shown in the accounts and the profits and loss account would reflect the depreciation accounted for in the accounts. If the profits are not large enough to wipe off depreciation, the profit and loss account would show a loss. Therefore, apart from proviso (b) to s. 10(2)(vi), neither the Act nor commercial principles draw any distinction between the various allowances mentioned in s. 10(2); the only distinction is that while the other allowances may be outgoings, depreciation is not an actual outgoing.

Bearing these two considerations in mind, if one looks at the language of proviso (b) to s. 10(2)(vi); the first question that arises is : What is the meaning of the expression "in the assessment of the assessee or if the assessee is a registered firm, in the assessment of the partners, full effect cannot be given to any such allowance in any year" ? It would be noted that the words used are "in the assessment of the assessee or the assessment of the partners". Taking the case of the partners of a registered firm, the assessment must be their individual assessments, i.e. assessments in which the profits from the firm and other sources are pooled together. The Legislature is clearly assuming that effect can be given to depreciation allowance in the assessment of a partner; the only way effect can

be given in the assessment of a partner is by setting it off against income, profits and gains under other heads. The learned counsel for the revenue tried to meet this inference by suggesting that what the Legislature contemplated was an assessment of those partners who were carrying on other business. But in our opinion this suggestion is unsound. What would happen if a partnership consists of four partners, two carrying on other business and two carrying on no other business, Mr. Sastri was unable to explain. Now, if this is the inference to be drawn from these words, it is quite clear that the words "no profits or gains chargeable for that year" are not confined to profits and gains derived from the business whose income is being computed under s. 10.

It appears that the Legislature accepted the interpretation placed by various High Courts on the Act as it stood before it was amended by Act 25 of 1953. In 1930, the Lahore High Court in Messrs Karam Ilahi Muhammad Shafi v. The Commissioner of income Tax, Delhi (3 Income Tax Cases 456; I.L.R. 11 Lahore 38.) held that depreciation on buildings and machinery can be set off against gains and profits accrued to the owner of those buildings and machinery from other sources such as rental from house property during the year in question. In A Suppan Chettiar & Co. v. The Commissioner of Income-Tax, Madras (4 Income Tax Cases 211; I.L.R. 53 Madras 702) the Madras High Court held that "where the profits and gains of a business are insufficient to cover the full depreciation allowance under section 10(2)(vi) of the Income-tax Act on the machinery, plant, etc., used for the purposes of that business, the excess depreciation can be set off against the profits and gains of other business or from other sources." In Ballarpur Collieries v. The Commissioner of Income Tax, Central Provinces (4 Income Tax Cases 255; A.I.R. 1930 Nag. 183), the Court of the Judicial Commissioner, Nagpur, held that the partners of the assessee, a registered firm owning collieries, were entitled to set off depreciation against the other income of the members of the firm under s. 24 of the Income Tax Act. In Laxmichand Jaipuria Spinning and Weaving Mills, In re (18 A.I.R. 919), the East Punjab High Court arrived at the same conclusion. The High Court further held that "the object of proviso (b) to sub-section (2) of section 24 is only to give preference to ordinary losses incurred by an assessee in regard to set-off over the loss which comes under clause (b) of the proviso to sub-section (2)(vi) of section 10. Where set off is to be given for different kinds of losses other than those due to depreciation such losses must be set off first and then the loss due to depreciation." In Ambika Silk Mills Co. Ltd. v. Commissioner of Income-Tax (22 I.T.R. 58, 65.) the Bombay High Court understood the effect of proviso (b) to s. 10(2)(vi) and proviso (b) to s. 24(2) as follows :

> "If a business was worked at a loss in any particular year, the loss can be set off against any other head under section 24(1); if the loss cannot be fully set off then it can be carried forward to the next year, but then it can be only set off against the profits of that particular business and that set-off would be permissible to the assessee for a period of six years only. After six years the right to set-off would come to an end. But in the case of depreciation and to the extent that the loss was caused by depreciation being not fully absorbed there would be no limit to the carrying forward of that depreciation, and that depreciation can be set off at any time so long as the business showed a profit in the future."

After the amendment, the same view has been taken in Commissioner of Income-Tax, Bombay City v. Ravi Industries Ltd. (49 I.T.R. 145.) by the Bombay High Court, and in Commissioner of Income-Tax v. Girdharilal Harivallabhadas Mills Co. Ltd. (3) by the Gujarat High Court. The only contrary view which has been placed before us is that of the Madras High Court in Commissioner of Income-Tax Madras v. B. Nagi Reddy (51 I.T.R. 178.), but we are unable to agree with the view expressed in the last case. The Madras High Court observed at p. 196 as follows :

> "In our opinion, the statute leads one to the irresistible conclusion that the depreciation allowance must be a charge only on the profits. The limit of the charge is the limit of the profits. The non-existence of profits will prevent the absorption of the allowance. There is no warrant for taking in and absorbing the depreciation allowance in the profit and loss account to work out a loss. If that were the true position, the provision for carrying forward the unabsorbed depreciation allowance would be wholly redundant, if not meaningless, in view of the specific provision for the carrying forward of losses."

The unabsorbed depreciation allowance is carried forward under proviso (b) to s. 10(2)(vi) and the method of carrying it forward is to add it to the amount of the allowance or depreciation in the following year and deeming it to be part of that allowance; the effect of deeming it to be part of that allowance is that it falls in the following year within cl. (vi) and has to be deducted as allowance. If the Legislature had not enacted proviso (b) to s. 24(2), the result would have been that depreciation allowance would have been deducted first out of the profits and gains in preference to any losses which might have been carried forward under s. 24, but as the losses can be carried forward only for six years under s. 24(2), the assessee would in circumstances have in his books losses which he would not be able to set off. It seems to us that the Legislature, in view of this, gave a preference to the deduction of losses first. But it is wrong to assume that s. 24(2) also deals with the carrying forward of depreciation. This carry forward having been provided in s. 10(2)(vi) and in a different manner; s. 24(2) only deals with losses other than the losses due to depreciation.

In conclusion, we agree with the High Court that the question referred to it should be answered in favour of the assessee. In the result, the appeal fails and is dismissed with costs.

Appeal dismissed.

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