

Commissioner of Income-Tax, Punjab

Vs

Lahore Electric Supply Co. Ltd

Civil Appeals Nos. 813 and 814 of 1963

(A. K. Sarkar, J. R. Mudholkar, R. S. Bachawat JJ)

25.11.1965

JUDGMENT

SARKAR J. –

The respondent is a company incorporated in 1912. The immediate object of the company was to acquire from the People's Bank of India Ltd. the license it had obtained from the Government for the supply of electricity to Lahore City. The company acquired that license in 1913, and the necessary plant and machinery for the generation and supply of electricity. Between 1923 and 1939, it acquired licenses for similar purposes in regard to various other places in different parts of India. All these licences were however either terminated or disposed of one by one and in 1942 the only licence which the company possessed was that in respect of the City of Lahore. About the end of 1942 or beginning of 1943, the Government of the then Province of Punjab acquired the company's undertaking in regard to the supply of electricity to the City of Lahore and on September 5, 1946, the company delivered its aforesaid undertaking with all assets to the Government. It was agreed that the company would pay to the Gover

In its assessment to income-tax for the years 1948-49 and 1949-50 the company claimed deduction of various amounts under section 10(2)(xv) of the Income-tax Act, 1922, on the basis that it had been carrying on business in the accounting years concerned and the expenses had been incurred solely for the purpose of that business. This contention was rejected by the Income-tax Officer. On appeal by the company to the Appellate Assistant Commissioner, certain deductions were allowed but that authority did not accept the contention that the company was carrying on business so as to come within section 10 of the Act. The company then took the matter up in further appeal to the Income-tax Appellate Tribunal. The Tribunal accepted the company's contention and granted it large deductions under section 10(2)(xv) of the Income-tax Act. The appellant-Commissioner of Income-tax requested the Tribunal to state a case to the High Court but that request was rejected. The appellant-Commissioner there after on August 20, 1958,

1. Whether, on the facts and in the circumstances of the case, the conclusion of the Appellate Tribunal that the assessee-company had not ceased to carry on business during the relevant accounting period is, in law, correct ?
2. If the answer to the first question be in the affirmative, whether all the expenses which the Tribunal has allowed are admissible under section 10(2) of the Income-tax Act ?

Accordingly the Tribunal stated a case to the High Court in regard to these two questions. The High

Court answered both the questions in the affirmative. Hence the present appeals by the Commissioner of Income- tax.

In this court the learned Additional Solicitor-General appearing for the appellant abandoned the second question. The only point, therefore that arises for decision in this appeal is whether, on the facts found, it could be said that the company had been carrying on business in the two accounting years.

As we have earlier stated, the Tribunal took the view that the company had not ceased to carry on business. The Tribunal observed that the question would depend on what the intentions of the company were. The High Court was of the same opinion. We also think that that is the correct view. This postulates that the company was not in fact carrying on any business, for, if it was, it would be superfluous to inquire whether the company intended to carry on a business. The courts below thought that the facts showed that the company intended to carry on business. The facts on which they relied were : (1) the company did not sell its undertaking as a going concern; (2) it continued in possession of all assets of its undertakings other than those appertaining to the Lahore electric supply undertaking; (3) it continued to hold deposits made by consumers of electricity supplied by the Lahore electric supply undertaking which had to be returned to them with interest; (4) it had no intention of going into liquidation;

In our opinion, none of the grounds mentioned in the preceding paragraph leads to the conclusion that the company intended to carry on business. The facts found make it abundantly clear that since 1942 the only business of the company was to work the Lahore electric supply licence. It stopped that business on September 5, 1946, when the undertaking was taken over by the Government. Thereafter, during the accounting years concerned, namely, 1947-48 and 1948-49, it had not started any other business. The mere fact that the company had not gone into liquidation would not establish that it had the intention to do business. If it were not so, then in the case of all trading companies it had to be held that they were always doing business. There is neither authority nor principle to support such a proposition. There was further no question of the company's going into liquidation in the accounting years, for, during that time, it had not received from the Government the entire amount due to it as compensation for

It would, therefore, appear that the business was closed and the company had not established an intention to resume it. That would be enough to show that no business was carried on and it would be irrelevant to inquire whether the business was permanently closed. We may add that we do not understand what was meant by saying that the company did not sell its undertaking as a going concern. The only going trading concern that it possessed was the Lahore electric supply undertaking and that it sold; it had no other commercial undertaking. After the sale of the Lahore electric supply concern all it did was to invest its moneys and the Tribunal has not found this activity to be a business.

The facts that the company had to pay the Government half share of the profits between November 27, 1942, and September 5, 1946, and that it had to return to the consumers the deposits made by them would not indicate that it was carrying on a business. It would be laying down strange law to hold that where a business has in fact ceased to be run, it must be deemed as continuing because the outstanding liabilities of that business had not been liquidated. The question whether the company was carrying on business arises only because, if it was, it would be entitled under section 10 to deductions from its business. Business as contemplated by that section is an activity capable of producing a profit which can be taxed. Payment of outstanding liabilities is not an activity which

can ever produce such a result. It cannot be said, therefore, that because liabilities of a closed business were outstanding, it has to be held that either the business was continuing or that an intention to resume business must be inferred.

Some reliance was placed in this connection on an observation of Lord Sumner in *Commissioners of Inland Revenue v. South Behar Railway Co.* There Lord Sumner observed, "If, as was held in *In re Dagnall* a married woman continues to carry on business for the purpose of 45 and 46 Vict., c. 75, section 1(5), as long as her trade debts remain undischarged, there would seem to be a presumption that a company continues to carry on business as long as it is engaged in collecting debts periodically falling due to it in the course of its former business." We are unable to hold that Lord Sumner intended to lay down that a business which is closed down is deemed to be carried on so long as its outstanding are being collected. *South Behar Railway's* case was concerned with a financing company whose only activity after the finances had been furnished was to receive from the Government by way of profits of the financing activity, earlier a certain proportion of the net earnings of the undertaking financed which was being managed.

The Tribunal did not hold that the company was in fact doing business or that anything that it did amounted to carrying on business. The onus of showing this was clearly on the company. All that it did was to refer to the sale of its Lahore electric supply undertaking to the Government and the listing of the assets of that undertaking and valuing it as the carrying on of business. This contention was rightly rejected by the Tribunal on the ground that the sale of the undertaking, though within its memorandum, was not its business which was really the working of the undertaking. It also seems to us that the condition of the country immediately following the partition is by itself irrelevant for deciding whether the company was doing business.

Learned counsel for the respondent contended that the Income-tax Officer's order showed that in one of the assessment years the company had received a certain amount as a result of a business of dealing in investments. The Tribunal however did not find this as a fact. Neither does it seem to us that the Income-tax Officer considered this income as business income though it described it as such, for he held that the company was not doing any business at all.

In our opinion, it must, therefore, be held that the company had ceased to carry on business and we would answer the first question in the negative. The appeals must be allowed with costs here and below and we order accordingly.

BACHAWAT J. –

These appeals by special leave raise the question whether the respondent-company was carrying on business during the accounting years 1947-48 and 1948-49, corresponding to the assessment years 1948-49 and 1949-50, and, therefore, entitled to deduction of expenses for carrying on the business under section 10(2)(xv) of the Indian Income-tax Act, 1922. The company was incorporated in 1912. In 1913, it acquired the licence to supply electric energy in Lahore and thereafter it acquired the licence to supply electric energy in Lahore and thereafter it acquired other licences for supply of electric energy at various other places. Before 1942, it disposed of all the licences other than the Lahore licence. Before other licences for supply of electric energy at various other places. Before 1942, it disposed of all the licences other than the Lahore licence. The Punjab Government took steps for the acquisition of the undertaking relating to the Lahore licence under the Defense of India Act and Rules, and

"In the meanwhile, however, your directors are considering if they could possibly purchase some manufacturing concern which might become an additional source of profit to the shareholders."

For the assessment year 1948-49 and 1949-50, the company claimed deduction of expenses for carrying on its business during the accounting years 1947-48 and 1948-49 under section 10(2)(xv) of the Indian Income-tax Act, 1922. The Income-tax Officer held that the company was not carrying on any business and totally disallowed contribution to employee's provident fund, pension and gratuity to old staff, value's remuneration, legal expenses, depreciation and income-tax provision, but the allowed a part of the salary paid to certain employees, rent, office expenses, interest, auditor's and director's fees. On appeal, the Appellate Assistant Commissioner held that, though there was some little business income, there was practically no business and he allowed in full the audit charges, director's fees and payment for interest, but he reduced the rent and establishment charges allowed by the Income-tax Officer. On further appeal by the company, the Appellate Tribunal recorded the following finding :

"Keeping in mind the entire facts and circumstances of this case, we have come to the clear conclusion that the assessee-company had not ceased to carry on its business."

On this finding, the Tribunal held that, in addition to the expenses allowed by the Appellate Assistant Commissioner, the whole of the contribution to provident fund, pension, gratuity, rent, depreciation, establishment charges and office expenses and the legal expenses for resisting the winding-up should be allowed. Under the orders of the Punjab High Court, the Tribunal referred the following questions of law for the decision of the High Court :

"(1) Whether, on the facts and in the circumstances of the case, the conclusion of the Appellate Tribunal that the assessee-company had not ceased to carry on business during the relevant accounting period is, in law, correct ?

(2) If the answer to the first question be in the affirmative, whether all the expenses which the Tribunal has allowed are admissible under section 10(2) of the Income-tax Act ?"

The Punjab High Court answered both the questions in the affirmative, and the Commissioner of Income-tax now appeals to this court by special leave. Counsel for the appellant conceded that if the first question is answered in the affirmative, the second question must also be answered in the affirmative. The sole question before us is, therefore, whether, on the facts found, the company had ceased to carry on business during the accounting years 1947-48 and 1948-49.

The memorandum of the company discloses the objects for which the company was constituted. If a question arises whether a particular activity of the company is a business activity, it is pertinent and relevant to inquire whether it is so regarded in its memorandum : see *Commissioners of Inland Revenue v. Korean Syndicate Ltd* *Karanpura Development Co. Ltd. v. Commissioner of Income-Axt Lakshminarain Ram Gopal & Sons v. Government of Hyderabad* In the instant case, the memorandum of the company discloses that its main purpose is to carry on the business of electric light and power company in all its branches, including generating and supplying electricity. Clause (4) the memorandum shows that one of its

subsidiary objects is to invest in stocks, shares, investment or securities of all classes and descriptions and to hold, sell, exchange or authorize dispose of and deal with them from time to time. A company may, of course, own shares and make investments, and still not carry on any business; but in this case th

It has been specifically found that the company was dealing in investments during the accounting year 1947-48 and that a surplus of Rs. 2,447 realised by the company from sale of its investments during the year was business income of the assessee : see paragraph 6 of the statement of case dated March 6, 1959, paragraph 4 of the order of the Appellate Assistant Commissioner dated April 18, 1951, and the last part of the order of the Income-tax Officer for the assessment year 1948-49, dated August 21, 1949. The order of the Income-tax Officer specifically stated that even the balance-sheet for the period ending March 31, 1947, showed that the difference on realisation of assets stood at Rs. 1,25,783, and it thus appeared that the company was dealing in securities. The revenue thus claimed to assess the surplus on the realisation of investments as the profits of a business under section 10, and its claim has been upheld. I fail to see how the revenue can take an inconsistent stand and claim that the activity of

The Tribunal also found that the entire business of the company was not sold to the Punjab Government as a going concern and the company continued to own and hold considerable assets not appertaining to the Lahore licence. The company sold and disposed of only its undertaking relating to the Lahore licence on September 5, 1946. Even then, the Punjab Government did not take up all the business debts and liabilities of the undertaking. The Company continued to pay interest on these deposits to the consumers. In paragraph 12 of its order dated December 8, 1951, the Tribunal observed, and, in my opinion, rightly :

"If payment of interest on consumer's deposits was a proper business expense in the preceding years, we do not see why or how its character changed in the years under review."

The Tribunal rightly pointed out that the activity of making lists and valuing the assets of the company for the purpose of ascertaining the price of the Lahore undertaking from the Punjab Government is not a business activity of the company. But, looking at the other facts and circumstances of the case and the relevant authorities on the point, the Tribunal came to the clear conclusion that the company had not ceased to carry on its business. There is enough material on the record to support this finding.

There is no set formula for determining whether in a given case a company is carrying on business. For the right understanding of the matter, one must import a little commonsense. From the shareholder's and the directors point of view, the company was undoubtedly carrying on business during the relevant accounting periods. From the popular point of view, what the company did during these years was a business activity. Again, if the question arose whether the company was carrying on business during these years for the purpose of section 20 of the Code of Civil Procedure, I have no doubt in my mind that the answer would be in the affirmative. From whatever point of view the matter is looked at, the conclusion is irresistible that the company was carrying on business during the relevant accounting years. There is ample material on which the Tribunal could come to this finding, and I see no reason for disturbing its finding.

In the result, the appeals are dismissed with costs.

ORDER. –

In accordance with the majority judgment, the appeals are allowed with costs here and below.

Appeals allowed.

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