O. RM. M. SP. SV. Firm

Vs

The Commissioner of Income-Tax-Madras

Civil Appeal No. 751 of 1965

(J. C. Shah, V. Ramaswami-I, V. Bharagava JJ)

14.10.1966

JUDGMENT

RAMASWAMI, J.

This appeal is brought, by certificate, against the judgment of the Madras High Court dated December 18, 1962 in T.C. No. 143 of 1960.

The appellant (hereinafter called the 'assessee') was a firm called O.RM.M.SP. SV. Firm which was registered under s. 26(A) of the Income-tax Act, 1922 (hereinafter called the '1922 Act'). Prior to the constitution of the firm, the partners were members of a Hindu undivided family. The family which consisted of Meyyappa Chettiar and his two brothers carried on money-lending business in India and in the former Federated Malaya States and it was assessed under the Indian Income-tax Act, 1918 (hereinafter called the '1918 Act'). There was a disruption of the joint family status on June 2, 1938, and thereafter the members of the family continued the business as partners. In the course of the assessment for the year 1939-40 it was claimed by Meyyappa Chettiar, one of the members of the family that having regard to the severance of joint family status, the income of the family from April 13, 1938 to June 2, 1938 was not liable to be taxed by reason of the provisions of s. 25(3) & (4). The Income-tax Officer accepted the fact of partition amongst the members of the family, but rejected the contention that the family was not liable to pay tax on the profits for the said period. The High Court ultimately called for a reference on the following question :

> "Whether the income of the family from 13th April 1938 to 2nd June 1938 is not liable to be taxed by virtue of Section 25(3) of the Indian Income-tax Act ?"

After receipt of the reference the High Court held that there was no discontinuance of the business within the meaning of s. 25(3). The view taken by the High Court was that when a Hindu undivided family carrying on a business, which was taxed under the 1918 Act, became disrupted and the members continued the business thereafter as partners, there could be no discontinuance but only succession by the firm of the business of the family. It was held in that case that it was the assessee-firm which took over the business of the Hindu undivided family. The firm was dissolved on March 2, 1952. In the assessment for the year 1952-53 the assessee applied for relief under s. 25(3) of the 1922 Act. The claim was rejected by the Income-tax Officer on March 7, 1956. The assessee preferred an appeal to the Appellate Assistant Commissioner who dismissed the appeal holding that in the case of business carried on in foreign territory the business as such is not assessed under s. 3 of the 1918 Act but only receipt of the income in British India is assessed and it cannot therefore be held that the foreign business of the appellant was charged to tax under the 1918 Act. The assessee took the matter in further appeal to the appellate Tribunal which considered that the assessee was

entitled to relief under s. 25(3) of the 1922 Act except for the income received from the house properties in Malaya. The appellate Tribunal accordingly allowed the appeal of the assessee in part. Both the assessee and the Department applied to the appellate Tribunal for reference of the questions of law to the High Court. The appellate Tribunal allowed the applications and stated a case to the High Court on the following questions of law :

> "(i) Whether the assessee is entitled to both the parts of the relief contemplated under section 25(3) of the Act in respect of foreign business at Penang, Ipoh and Kambar ?
>
> (ii) Whether the applicant is also entitled to relief under section 25(3) of the Act with regard to rental income from house properties owned by the foreign firm which was discontinued in the year of assessment."

The appellate Tribunal also referred another question for the opinion of the High Court but it is not the subject-matter of the present appeal.

The High Court held that the assessee was not entitled to relief under s. 25(3) of the 1922 Act and accordingly answered both the questions in favour of the Department. The view taken by the High Court was that the foreign business of the assessee cannot be deemed to have been charged under the provisions of the 1918 Act because the assessee was only taxed on remittances received from the profits of the foreign business and there was no tax on the foreign business itself under the 1918 Act. The High Court accordingly reached the conclusion that the assessee was not entitled to relief under s. 25(3) of the 1922 Act.

Section 25(3) of the 1922 Act is to the following effect :

> "25. (3) Whether any business, profession or vocation on which tax was at any time charged under the provisions of the Indian Income-tax Act, 1918 (VII of 1918), is discontinued, then, unless there has been a succession by virtue of which the provisions of sub-section (4) have been rendered applicable no tax shall be payable in respect of the income, profits and gains of the period between the end if the previous year and the date of such discontinuance, and the assessee may further claim that the income, profits and gains of the previous years shall be deemed to have been the income, profit and gains of the said period. Where any such claim is made, an assessment shall be made on the basis of the income, profits and gains of the said period, and if an amount of tax has already been paid in respect of the income, profits and gains of the previous year exceeding the amount payable on the basis of such assessment, a refund shall be given of the difference."

Under this section exemption from liability to pay tax in respect of the income, profits and gains may be claimed by an assessee if the business is one in respect of which tax was charged at any time under the 1918 Act, and the business is discontinued - there being no succession by virtue of which the provisions of sub-section (4) of s. 25 have been rendered applicable. Section 25(3) however, applies even if the person assessed under the 1918 Act was different from the person who claims relief under that section provided the former was the predecessor-in-interest of such person in relation to the business. The reason for enacting s. 25(3) was that under the 1918 Act, income-tax was levied by virtue of s. 14(2) of the 1918 Act, on the income of the year of assessment. Tax was, therefore, levied in the financial year 1921-22 on the income of that year. By the 1922 Act the basis of taxation was altered and by s. 3 of that Act, charge for tax was imposed upon income of the

previous year. When the 1922 Act was brought into force on April 1, 1922, two assessments in respect of the same income for the year 1921-22 had to be made. The income for 1921-22 was accordingly charged to tax twice; it was charged under the 1918 Act and it was also charged to tax under s. 3 of the 1922 Act read with the appropriate Finance Act, resulting in double taxation in respect of the income for the year. But with a view to make the number of assessments equal to the number of years during which the business was carried on, the legislature enacted the exemption prescribed by s. 25(3). This benefit was however restricted only to the income, profits and gains of business, profession or vocation on which tax had been charged under the provisions of the 1918 Act. By enacting s. 25(3) the legislature intended to exempt the income, profits and gains resulting from the activity styled business, profession or vocation from tax when the business, profession or vocation is discontinued if tax was charged in respect thereof under the 1918 Act.

The first question to be considered in this appeal whether the assessee is entitled to both parts of relief contemplated under s. 25(3) of the 1922 Act in respect of the foreign business at Penang, Ipoh and Kambar. The controversy between the parties turns on the question whether the foreign business of the assessee was at any time charged under the provisions of the 1918 Act. It has been found by the appellate Tribunal that the assessee was taxed on remittances received from and out of the profits of the foreign business. The finding of the Appellate Assistant Commissioner is stated in these terms :

> "The entire profits of the foreign business came to be assessed in the hands of the appellant under the 1918 Act, not because it was a business income but because such income had been remitted into British India. Therefore, in fact also it is not the foreign profits of a business that has been charged to tax but only the remittance which in the particular case was not less than the profits of the year."

We have therefore to proceed on the footing that the assessee received the entire profits of the foreign business in British India and the entire profits were assessed to income-tax in the hands of the assessed under the 1918 Act. It is necessary, at this stage, to set out the relevant provisions of the 1918 Act.

Section 3, the charging section stated as follow :

> "3. (1) Save as hereinafter provided, this Act shall apply to all income from whatever source it is derived, if it accrues or arises or is received in British India, or is, under the provisions of this Act, deemed to accrue or arise or to be received in British India.
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> #. . . . . ."##

Section 5 mentioned the classes of income chargeable to income-tax and reads as follow :

> "5. Save as otherwise provided by this Act, the following classes of income shall be chargeable to income-tax in the manner hereinafter appearing, namely -
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> #(i) Salaries.(ii) Interest on securities.(iii) Income derived from house property.(iv) Income derived from business.(v) Professional earnings.(vi) Income derived from other sources."##
>
> Section 9 of the 1918 Act enumerated the permissible deductions in the computation

of the profits of the business. The question for determination is whether the foreign business of the assessee was at any time charged under the provisions of s. 3 of the 1918 Act. It has been found in this case that the entire income of the foreign business was remitted to the assessee and tax imposed on that income under the 1918 Act. We are of the opinion that in the context of these facts the foreign business of the assessee must be held to be charged under the provisions of the 1918 Act within the meaning of s. 25(3) of the 1922 Act. It is manifest that by s. 3 of the 1918 Act the charge was made on the receipt of income in British India and as the income received by the assessee was derived from the foreign business and was in relation to the foreign business it must be taken that there was an assessment to tax on the foreign business within the meanings of s. 25(3) of the 1922 Act. In other words, the tax under the 1918 Act was charged upon the assessee in respect of his activity styled 'foreign business' and in relation to it and it must hence be taken, upon the facts found by the appellate Tribunal in this case, that the foreign business of the assessee was charged under the 1918 Act within the meaning of s. 25(3) of the 1922 Act. The High Court has taken the view that the foreign business of the assessee was not charged under the 1918 Act because what was taxed was the remittances received by the assessee from the foreign business and not the foreign business itself. In taking this view, the High Court has followed its previous decision in Commissioner of Income-tax, Madras v. S.V.R.M. Palaniappa Chettiar and Others (20 I.T.R 170.) in which it was held that the words "on which" in s. 25(4) of the 1922 Act cannot be interpreted as meaning "with reference to which" and that in order to claim and avail the benefit under s. 25(4) the tax clearly should be charged on the business as such under the 1918 Act. At page 173 of the Report Satyanarayana Rao, J. stated as follow :

"The relief under sub-clause (4) is permissible only if the tax on the business was charged under the provisions of the Indian Income-tax Act, 1918. If the foreign business at Muor was not and could not have been charged under the Act and the share in the profits of the family from that foreign business was charged under section 3 only on the receipt in British Indian, can it be said that the charge so made was a charge of a tax on the foreign business. The income received by the joint family could not have been charged under the head 'income derived from business' but only as a receipt under section 3. The argument, however, on behalf of the assessee by his learned Advocate Mr. Rajah Iyer was that the words "on which tax was at any time charged" should be construed as meaning "with reference to which tax was at any time charged." In other words, the contention is that the income derived by the assessee was in relation to a business and therefore the assessment of the income must be treated as an assessment of the business. No doubt, under the provisions of the Income-tax Act, the tax is payable by an assessee but the assessment of the tax is on the basis of various heads of income derived by the assessee one of which is business. It cannot, therefore, be said that because tax was payable by the assessee on the profits received from a business in a foreign territory such assessment is an assessment of the business."

In our opinion, the view adopted by the High Court in Commissioner of Income-tax, Madras v. S.V.R.M. Palaniappa Chettiar and Others () must be taken to be impliedly over-ruled by the recent decision of this Court in Commissioner of Income-tax. Bombay City-1 v. Chugandas & Co. ([1964] 8 C.S.R. 332.) in which the question was whether the interest on securities formed part of the

assessee's business income for the purpose of the exemption from tax under s. 25(3) of the 1922 Act. It was held by this Court that the assessee was entitled to exemption under s. 25(3) in respect of interest on securities as well, and there was no reason to restrict the condition of the applicability of the exemption under s. 25(3) only to income on which the tax was payable under the head "Profits and gains of business, profession or vocation". It was further observed in that case that tax is charged under the Income-tax Acts on specific units, such as, individuals, Hindu undivided families, companies, local authorities, firms and associations of person etc. and business, profession or vocation is not a unit of assessment. When, therefore, s. 25(3) enacts that tax was charged at any time on any business, it is intended that the tax was at any time charged on the owner of any business. If that condition be fulfilled in respect of the income of the business under the 1918 Act, the owner or his successor-in-interest in relation to the business, will be entitled to get the benefit of the exemption under it if the business is discontinued. We are accordingly of the opinion that the High Court was in error in holding that the foreign business of the assessee was not charged under the provisions of the 1918 Act. The first question must therefore be answered in favour of the assessee and it must be held that the assessee is entitled to both parts of relief contemplated under s. 25(3) of the 1922 Act in respect of the foreign business at Penang, Ipoh and Kambar.

The second question of law arising in this appeal is whether the assessee was entitled to relief under s. 25(3) of the 1922 Act with regard to the rental income from house properties owned by the foreign firm which was discontinued in the year of account. A similar question was the subject-matter of consideration in Commissioner of Income-tax, Bombay City-I v. Chugandas and Company ([1964] 8 S.C.R. 332.) which has already been referred to. In that case, the assessee firm, a dealer in securities holding securities as its stock-in-trade, had been charged to tax under the 1918 Act, in respect of business. It received Rs. 4,13,992 and Rs. 1,01,229 as interest on securities in the years 1946 and 1947 respectively. The firm discontinued its business on June 30, 1947. The question at issue was whether the interest on securities formed part of the assessee's business income for the purpose of the exemption from tax under s. 25(3) of the 1922 Act. It was held by this Court that the assessee was entitled to exemption under s. 25(3) in respect of interest on securities as well. It was pointed out that there was no reason to restrict the condition of the applicability of the exemption under s. 25(3) only to income on which the tax was payable under the head "Profits and gains of business, profession or vocation". The exemption under s. 25(3) is general. It was explained by this Court that the heads of income described in s. 6 of the 1922 Act, and further elaborated for the purposes of computation in ss. 7 to 10 and 12, 12A, 12AA and 12B, are intended merely to indicate the classes of income. The heads do not exhaustively delimit sources from which income arises. Business income is broken up under different heads only for the purpose of computation of the total income. By that braking up the income does not cease to be the income of the business, the different heads of income being only the classification prescribed by the Income-tax Act for computation. The ratio of this decision applies to the present case and it must accordingly by held that the assessee is entitled to relief under s. 25(3) of the 1922 Act with regard to the rental income from the house properties owned by the foreign firm which was discontinued in the year of account.

For these reasons the judgment of the Madras High Court is set aside and this appeal must be allowed with costs.

R.K.P.S.

Appeal allowed.

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