BOMBAY HIGH COURT

Saifudin Alimohamed

Vs.

Commissioner of Income-tax

Income-tax Ref. No. 22 of 1953

(Chagla, C.J. and Tendolkar, J.)

10.09.1953

JUDGMENT

Chagla, C.J.

1.The question raised on this reference is of some difficulty and complexity and the difficulty and complexity is by no means resolved by the Taxing Department taking a particular view of the law at one stage and taking a different view at another.

2. The facts are few and simple. One Hydarali Hasanally died in January 1944 leaving behind him two minor daughters. He left some immoveable property and he also left behind him a business which was the business of a restaurant called the New Coronation Durbar Hotel. Mr. Justice Blagden on May 18, 1944, appointed two guardians of the two minors and he authorized the guardians to continue the business of the New Coronation Durbar Hotel and he also ordered that the guardians should collect and recover the income, rents and profits of the hotel and the immoveable properties and to pay out of the income all necessary expenses of the management, of the hotel and all the collection and other outgoings in respect of the business and immoveable properties and pay certain maintenance every month for the education and benefit of the minors, and he finally ordered that after defraying all the expenses aforesaid the guardians were to deposit twice every year, viz. at the end of April and October with the Accountant General the share of the minors in the balance of income, rents and profits from the business and the immoveable properties, and the Accountant General was to open an account in the name of the two minors and invest the moneys and keep the amount received to the credit of the two minors. The two guardians made a return in respect of the income from the property and from the business of the hotel. The business income was assessed by the Income-tax Officer at Rs. 54,979 and the property income at Rs. 4,488. The Income-tax Officer assessed both the incomes as having been earned by an association of persons constituted by the two guardians and this association of persons was called upon to pay the tax on both the business income and the

property income. In appeal the Appellate Assistant Commissioner held that the case was governed by Section 41 of the Act and the total income shown by the guardians should be distributed between the two beneficiaries and the tax should be levied accordingly on the moiety of the income. The Department went in appeal against the Appellate Assistant Commissioner's order only to the extent of the business income. They accepted the decision of the Appellate Assistant Commissioner with regard to the Income from the property. The Tribunal reversed the decision of the Appellate Assistant Commissioner and came to the conclusion that the business income was rightly taxed by the Income-tax Officer and the Appellate Assistant Commissioner was wrong in the view chat he had taken. The view of the Tribunal as expressed in the order that they passed was that the business was carried on jointly by the guardians of the minors and therefore it could be said that the business was earned on by an association of persons, and as the income was derived from that business the income was rightly taxed as a unit and could not be divided between the two minors as the income from property had been done. The assessee asked the Tribunal to refer the matter to the Court and that has been done by the Tribunal, and the question of law which they have raised is :

> "Whether on the facts and in the circumstances of the case, the income of Rs. 54,979 arising from the carrying andn of the business by the guardians of the minors is rightly charged to tax under Section 3 read with Section 10 of the Indian Income-tax Act in the hands of the guardians as an association of persons ?"

In our opinion this question of law which has been raised on a suggestion by the Department does not really bring out the controversy between the parties. The real question is the question suggested by the assessee and in respect of which a notice of motion has been taken out, and the question is :

> "Whether each minor being entitled to one half of the properties and business the income of each minor should not have been separately assessed on the minor by her guardians and managers the applicants ?"

3. In the question raised by the Tribunal it does not appear that the assessment proceeded under Section 40 or Section 41 of the Act. As we shall presently point out, that was the very basis of the assessment made by the Department and therefore the question whether the Department was right in the way it had taxed the business income can only be decided by a consideration of the provisions of Section 40 or Section 41 of the Indian Income-tax Act. At no time was it the case of the Department that they were assessing the guardians to tax under Section 10 read with Section 3 of the Act irrespective of the provisions of Section 40 or Section 41. On the contrary, the order of the Income-tax Officer makes it perfectly clear that the guardians were assessed to tax by reason of the fact that they were guardians and by reason of the liability imposed upon them under Section 40.

4. Before we consider the authorities that were cited at the bar, we will look at the provisions of the Act itself. The charging section is Section 3 and it is clear that the assessable entity under the Indian Income-tax Act is not necessarily the same as a legal entity. A minor can be an assessable entity and so also can be an association of persons which may include minors or even all of whom may be minors. Chapter III in which appears Section 10 deals with taxable income and the computation of that income, and Section 10 deals with the income under the head of business, and Section 10(1) provides that the tax shall be payable by an assessee under the head "profits and gains of business, profession or vocation" in respect of profits or gains of any business, profession or vocation carried on by him. Therefore, looking to the plain language used by the Legislature, what has been emphasised in this section is the fact of a business being carried on by the assessee. It is the assessee who carries on a business who is liable to pay tax under the head of business. It is rather significant to notice the difference in language in Section 10 and Section 9. Section 9 deals with tax under the head of property and in at tax is payable by an assessee who is the owner of the property. So in the case of property what is emphasized the Legislature is ownership, in the case of business what is emphasized is not the ownership of the business, but the fact of the business being carried on by the assessee. Now, if the intention of the Legislature was that tax under the head of business should be paid by every assesses who owns a business, irrespective of the question whether he carries it on or not, nothing would have been simpler for the Legislature than to have reproduced the same language in Section 10 as is to be found in Section 9. The Legislature could have provided that the tax shall be payable by an assessee in respect of the profits and gains of any business owned by the assessee.

5. Therefore, we have to give proper effect to the language used by the Legislature in Section 10 and the emphasis placed by the Legislature on the fact of a business earned on by the assessee. We agree with Sir Nusserwanji on behalf of the Department that it is necessary under Section 10 that an assessee should physically or with his own hands carry on a business before he becomes liable to pay tax, He may employ an agent, he may not even be present in the place where the business is carried on, he may take a rather casual interest in his business, but that would not permit him to contend that he is not carrying oil the business and he is not liable to pay tax in respect of the profits derived from that business. But an assessee must have the right to carry on a particular business before he can be called upon to pay the tax under Section 10 and the business most be carried on in the exercise of that right. If the owner of a business is incapacitated from carrying on the business and he has no right to carry on the business, then although he may be the owner of the business he would still not be liable to pay tax under Section 10 because he is not carrying on the business. The incapacity may be caused by natural reasons or by intervention of the Court. A person may be a minor, he may be a lunatic, and as such although he may own a business or inherit a business he would be incapable in law of carrying on that business. On the other hand, the Court may intervene and deprive the owner of the right of carrying his own business and authorize someone else to carry on the business for him, in which case the person who would be carrying on the business would not be the owner but the person appointed or authorized by the Court.

6. In this particular case the father of the minors was carrying on the business and as such he was liable to pay tax under Section 10. On his death the business was inherited by his two daughters. They were both minors. It is nobody's case that they ever carried on the business or could carry on the business. Therefore, the Court intervened and the Court appointed the two guardians and directed and authorized the two guardians to carry on the business. The minors had nothing whatever to do with the carrying on of the business. They were, as it were, immobilized and their only interest lay in the share that they would get after the business had been carried on after it had made profits and after all the outgoings had been paid and the net profits ascertained and deposited with the Accountant General. But the carrying on of that business and deriving profits from that business was left to the guardians and was not done by the minors. Therefore, it could have been legitimately said by the taxing department that the guardians constituted an association of persons and they have carried on business and they have earned profits and those profits are liable to tax under Section 10. But the Department did not choose to proceed directly under Section 10. it chose to proceed under Section 40 or Section 41 and attempted to tax the guardians not in respect of the business carried on by them in their own right, but to tax them as guardians who had carried on business on behalf of the minors and who had received income from the business on behalf of the minors, and what we have to consider is whether it is possible for the Department to contend that when business is carried on by guardians, the minors are liable to pay the tax in respect of the income earned under Section 10 and the guardians can be made to pay that tax under Section 40 or Section 41 of the Act.

7. Now, turning to these two Sections 40 and 41, they are undoubtedly machinery sections and they do not impose any new liability, nor do they in any way reduce or minimize the liability which is already there upon the assessee under the other provisions of the Income-tax Act. Section 40 deals with a case of a minor, lunatic or idiot and where a guardian or trustee is appointed, and what it provides is that when you have a guardian or a trustee and he receives or is entitled to receive on behalf of his ward or beneficiary any income, he is liable to pay tax upon that income in the like manner and to the same amount as it would be leviable upon and recoverable from any such beneficiary if of full age and sound mind and in direct receipt of such income, profits or gains, and all the provisions of this Act shall apply accordingly. Therefore, to use simple language, Section 40 imposes a vicarious liability upon a guardian and trustee and that vicarious liability is co-extensive with the liability of the ward or the beneficiary of whom the assessee is the guardian or the trustee. It is not the liability of the guardian or the trustee himself; it is the liability of the minor or the beneficiary. But the law provides a machinery whereby the taxing department by this option, instead of recovering the tax from the minor or the ward or the beneficiary, may recover it from the guardian or the trustee. Sub-Section (2) of that section deals with the case of a trustee or agent of a person not resident in the taxable territories who is not a minor, lunatic or idiot. In that case also it imposes a vicarious liability upon the trustee or agent of such person. Then we come to Section 41 and Section 41(1) deals with two cases, viz., the cases of trustees appointed under a trust deed in writing and also persons

appointed to manage property on behalf of another by an order or under an order of a Court, and when such an appointment is made or when such a trustee is appointed, a similar liability is cast upon the trustee or the persons appointed by the Court. Then there is a proviso to Sub-Section (1) and that lays down that

> ".....where any such income, profits or gains or any part thereof are not specifically receivable on behalf of any one person, or where the individual shares of the persons on whose behalf they are receivable are indeterminate or unknown, the tax shall be levied and recoverable at the maximum rate : but, where such persons have no other personal income chargeable under this Act and none of them is an artificial juridical person, as if such income, profits or gains or such part thereof were the total income of an association of persons."

So this proviso to Sub-Section (1) gives the right to the taxing department to levy tax at the maximum rate where a trustee does not specifically receive income on behalf of his beneficiary or where the shares of the beneficiaries are indeterminate or unknown. Therefore, Mr. Palkhiwala is right when he urges that under Section 41, unless a case falls under the proviso just referred to, what can be charged in the hands of a trustee or a person appointed by the Court is only the share of the income of the beneficiary coming into his hands. It is only when the proviso applies that the tax can be levied on the income coming into the hands of the trustee at the maximum rate. Mr. Palkhiwala has attempted to argue that the present case falls under Section 41 because we have an order of this Court and the guardians have been appointed to manage property on behalf of the minors. In our opinion it is clear that Section 40(1) deals with a specific case of a guardian, and Section 41 deals with a wider class of cases where the Court may appoint a person who may not be appointed a guardian to manage the property of the minor, and it would be contrary to all canons of construction to put a case under a section which deals with general provisions when the Legislature has provided a specific section to deal with a specific case. As we are dealing with the case of a guardian, and Section 40(1) was enacted in order to deal with the specific case of a guardian, there is no reason why we should consider Section 41, and therefore in our opinion it is Section 40 that applies to the facts of this case and not Section 41.

8. Now, inasmuch as the Department contended that the assessees were liable to pay tax on the business income as a whole and they proceeded under Section 40, Sir Nusserwanji had to satisfy us that under Section 40(1) the guardians in this case were liable to pay tax on the income of the business earned as a whole by the guardians carrying on that business. What has been emphasized by Sir Nusserwanji is that Section 40 not only permits the taxing Department to levy tax and make it recoverable from the guardian in like manner and to the same amount as it would be leviable upon and recoverable from a beneficiary, but it further goes on to say

> "as if the beneficiary was of lull age or sound mind and in direct receipt of such income, profits or gains."

Therefore, according to Sir Nusserwanji we must assume that the minors were of full age and we must assume that they were in direct receipt of the income which has been received by the guardians, and if we make that assumption, according to Sir Nusserwanji it is clear that in that case we must come to the conclusion that the income derived by the guardians by carrying on the business would have been derived by the minors if they were of full age. The only legal fiction created by Section 40 is the fiction of minors being majors at the date when their guardians received the income on their behalf. Sir Nusserwanji wants us to add a further fiction which the section does not warrant and that additional fiction is that not only the minors were majors at the date when the guardians received the income, but the minors carried on the business from which the income was derived. Now, discarding the attitude taken up by the taxing department, Sir Nusserwanji has asked us to consider that the minors themselves constitute an association of persons and we must assume that they carried on the business being of full age, which business was being can led on by guardians because they were minors. In the first place, in order to constitute a body of persons into an association of persons, there must be some unity of purpose, and there is nothing whatever to show that the minors did ever conceive of any unity of purpose in relation to this business. But what is more difficult and almost insurmountable in the way of Sir Nusserwanji is that even if the minors were majors at the relevant date, they could not have carried on the business because there was a legal impediment in their way. So long as the order of Mr. Justice Blagden stood, the only persons who had the right to carry on the business were the guardians and not the minors. The other difficulty in the way of Sir Nusserwanji is that under Section 40 what the guardians were entitled to receive on behalf of the minors was not the income from the business carried on by them, but the share in the profits ascertained after taking into consideration all outgoings and necessary expenses. It is possible - indeed it is probable - that the profits of the business under Section 10 for the purpose of tax would be entirely different from the profits of the business in which the minors would have a share by reason of they being their father's heirs. Whereas the profits of the business under Section 10 would be arrived at by the mode of computation laid down in the Act itself, the net profits in which the minors would have a share would be arrived at by a computation which would be on a commercial basis and which in ail probability would not be identical with the mode of computation laid down in the Indian Income-tax Act. Therefore, it is fallacious to suggest that the income which the guardians earned by reason of carrying on the business was the income to which the minors, were entitled and which income was received by the guardians on behalf of the minors. The income which the guardians earned was an income derived by them by reason of a business which they carried on in their right pursuant to the order of the Court. The income to which the minors were entitled was an entirely different kind of income which would be ascertained after the business was carried on, profits made and net profits ascertained. Sir Nusserwanji says that Section 40 does nothing more than to enable the taxing Department to tax income of a business carried on by a guardian on behalf of the minor. In our opinion such a contention is not borne out by the language of Section 40.

9. Therefore, as the facts stand on this reference, it was open to the Department to have assessed the income of the guardians under Section 10 oil the basis that the particular business was carried on by the guardians in their own right, and the taxing Department could have taken up the stand that they had no concern with what the guardians did with the profits after they had paid the tax on the income from the business; or it was open to the Department to proceed against the guardians under Section 40(1) and to tax in their hands only that income which they had received on behalf of the minors. Rightly or wrongly, fortunately or unfortunately, the Department has chosen to take recourse to the second alternative, and if they have taken recourse to the second alternative, then it is not open to the Department now to suggest that the guardians should be taxed directly under Section 10 and not under Section 40(1) because it must again be emphasised that the liability of the guardians under Section 10 would have been a very different liability from their liability under Section 40. Whereas their liability under Section 10 would have been personal and direct, in respect of the business which they themselves carried on, their liability under Section 40 is indirect and vicarious, it is indeed not their liability at all because they are discharging the liability which the minors have, to pay tax upon their income.

10. Turning to the authorities cited at the bar they are not at all easy to understand, with, respect, or to explain. But we will briefly look at them in the light of what we have already said in our judgment as to the true construction of Sections 10, 40 and 41. The first is the decision reported in - *'Commissioner of Income Tax, Bihar and Orissa v. Habibur Rahman[1]',* That, was the case of a mutawalli who executed a deed of wakf end dedicated the income from his business, and he and the members of his family, his children and descendants were to benefit under this trust. It was found by the tribunal that the persons who were entitled to share in the profits, were 24 in number, and the Patna High Court held that the assessee mutawalli should be taxed on the basis of profits failing

[1] AIR 1945 Pat 494

to the share of each beneficiary and not on the footing of all the beneficiaries constituting an association of persons, and held that the first proviso to Section 41(1) was inapplicable. Therefore, the view taken by the Court was that Section 41 applied and the trustee or mutawalli was liable to pay tax in respect of each of the shares of the beneficiaries which he received. What was emphasized by Mr. Palkhiwala was that this, was a case where the income was derived from business and yet the tax was not on the income of the business as a unit but it was on the specific share of each of the beneficiaries which he had in the profits of the business. Now, this is only a decision on the applicability of the proviso to Section 41. The Department did not proceed to assess any person who was carrying on the business under Section 10, and therefore we do not find in this judgment any discussion as to the true interpretation of Section 10.

11. The other decision is - *'S.C. Mazumdar v. Commissioner of Income Tax[2]',* That was the case of a receiver who was the assessee and he was appointed receiver of the Trigunait Brothers' Estate in a partition suit, and the Patna High Court came to the conclusion that the assessment should be made against the receiver under Section 41(1). It held that the Trigunaits had

dissociated themselves from each other because the partition suit was pending, and therefore it could not be said that they were an association of persons carrying on the business. It says that the business was being carried on by the receiver and they further observe that the assessment should have been made and could only be made on the receiver. But the principle of this decision seems to be that when the receiver is carrying on business on behalf of parties who have ceased to be an association of persons and of whom it could not be said that they were in a position to carry on the business or had any right to carry on the business, and if the assessment is under Section 41, then the assessment could only be made on the receiver in respect of the share of each of the parties and not on the income of the business as a whole. If this is a correct reading of this judgment, then, it is in conformity with the view that we have taken.

12. The third case is - *'Commissioner of Income Tax. Madras v. J.V. Saldhana*[3]*',* In that case the widow of Saldhana became entitled along with her six minor children to the estate of her deceased husband and among the property was a third share in a firm of coffee curers and sellers. The widow obtained letters of administration to the estate of the deceased husband and got herself recognised as the partner in place of her deceased husband and continued' to carry on the business in the same manner as had been conducted by the deceased, and the Madras High Court held that a single assessment should be made on the widow under Section 10(1) of the Act on the entire income from the business carried on by her. This case has been strongly relied upon by Sir Nusserwanji, but it is pertinent to point out that in this case the assessment was not under, Section 40 or 41. It was a direct assessment upon the widow as the person who carried on the business and who earned profits from that business. Certain difficulties are created by this decision because it is difficult to understand why the widow alone should have been assessed to the profits of this business, if, as seems to have been held by the Court, the business was carried on by an association of persons including herself and the other heirs of her deceased husband. But if the decision merely lays down that inasmuch as the widow was the person who was actually carrying on the business and she was not carrying it on behalf of herself and the other heirs out in, her own right, then again the

[2] AIR 1948 Pat 385

[3] AIR 1932 Mad 378 (SB)

decision is in conformity with the view that we have expressed. But if the view is taken that not only the widow but the other heirs also had the right to carry on this business, then the mere fact that Mrs. Saidhana was in physical charge or control of the business would not make any difference to the liability to pay tax under Section 10 of the others, who, although they did not actually share the carrying on of the business with the widow, had the right to carry on the business as much as the widow herself. It may also be pointed out with respect to the learned Judges, that they seemed to have taken the view that a business under the Indian Income-tax Act is a unit of assessment and that the business as such can be assessed under Section 10. That clearly is not the true legal position, what is assessed under the Indian Income-tax Act is not a business, but the persons who carry on the business.

13. The other case that was referred to at the bar is a decision of the Punjab High Court in - *'Hotz*

Trust v. Commissioner of Income Tax, Punjab[4]*',* There, under a testamentary trust deed the trustees were given full powers to carry on the hotel business of the testator; they had also the power to extend the business, accumulate income, borrow capital and to distribute the profits and accumulated income among the beneficiaries; and what the Punjab High Court held was that the trustees were an association of individuals within the meaning of Section 3 of the Income-tax Act carrying on the business, assessable as such a unit in respect of the profits of the business in their hands. In this case also the learned Judges point out at pp. 930 and 931 that admittedly Section 40 of the Act, which deals with the liability of a trustee in certain specified special cases, does not apply to the facts of the case; and the income-tax authorities held the trustees liable under the general provisions of the Act. Therefore, there we had a case of a direct assessment upon the trustees who were actually carrying on the business and were assessed under Section 10 of the Act. An opinion is expressed that (at p. 933) :

> "..... .Section 40 is merely a machinery section, making the trustee liable for beneficiaries in certain cases where the beneficiaries are difficult or impossible to get at, and where the trustee acts as a conduitpipe for the conveyance of the income to the beneficiaries. It does not affect the charging Sections 3 and 10 of the Indian Act under which the trustees as an association of individuals, carrying on a business, are liable to be assessed in respect of the gains of the business carried on by them."

Therefore, the view taken was that a distinction must be made between trusts where the trustees merely act as conauitpipes and trusts where trustees take an active part in the earning of the income. Whether that distinction is well founded or not, it is unnecessary to decide or to express an opinion upon. But the judgment clearly takes the same view as we have done that where trustees re carrying on business in their own right, then the proper way to assess them in respect of the income of the business is directly under Section 10 and not under the machinery Section 40 or 41. The judgment also cites with approval the observation of Viscourt Cave - *'A.W. Williams v. W.M.G. Singer*[5]*',* at p. 411, to the following effect (at p. 933) :

> "The fact is that, if the Income-tax Acts are examined, it will be found that the person charged with tax is neither the trustee nor the beneficiary as such, but the person in actual receipt and control of the income, which it is sought to reach."

[4] ATR 1930 Lah 929

[5] 1921-7 Tax Cas. 387

Whether this observation is true of all the provisions of the Indian Income-tax Act or not we cannot say, because Viscount Cave was not considering the Indian Income-tax Act, but it is certainly true of Section 10 which assesses to tax only that income which has been received by persons who carry on business and in that sense it may be said that they are in receipt and control of the income of the business. Therefore, on a review of these authorities, it is clear that there is no decision to which our attention has been drawn in which a person not carrying on the business in the sense in which we have indicated has been assessed to tax under Section 10, and as the

whole foundation of the argument advanced before us by Sir Nusserwanji is that the persons who carry on the business within the meaning of Section 10 are an association of persons constituted by the minors, the contention must obviously fail. The Department must fail in either view of the case. If we take the view as was advanced before the tribunal and before the other taxing authorities that the persons who carry on the business are the guardians who constitute an association of persons because they have not been assessed directly under Section 10 but they have been assessed under Section 40, the Department must fail. If, on the other hand, the view is as now urged that the persons who should be assessed are the minors because they carry on the business as the business belonged to them, then also the Department is bound to fail, because in this particular case it is the guardians who carry on the business under the order of the Court and not the minors.

14. Therefore, the assessee is entitled to succeed and the question we will answer is the question which the assessee has raised on the notice of motion, and the question is whether each minor being entitled to one half of the properties and business the income of each minor should have been separately assessed on the minor by her guardians and managers the applicants; and the answer we will give is in the affirmative. We have not thought it necessary to call for a statement of the case with regard to this question, because the facts submitted to us on this reference are sufficient to answer the question raised by the assessee.

15. The Commissioner must pay the costs of the reference including the costs of the motion.

Reference answered.