PATNA HIGH COURT

Motipur Sugar Factory Ltd

Vs

Commissioner of Income Tax

Misc. Judicial Case No. 402 of 1954

(Ramaswami and Kamla Sahai, JJ.)

24.03.1955

JUDGMENT

Kamla Sahai, JJ.

1. In this case the assessee is a private limited Company carrying on business in the manufacture of sugar and molasses out of Sugarcane. The assessment year is 1951-52 and the accounting year corresponds to the period from 1-10-1949 to 30-9-1950.

2. The purchase of Sugarcane on behalf of the assessee was governed by the Bihar Sugar Factories Control Act, 1937, (Bihar Act 7 of 1937) and the Bihar Sugar Factories Control Rules 1938. In accordance with those rules the assessee company was required to set up purchasing centres for sugarcane and to locate weigh bridges at the purchasing centres. The assessee company was also required to purchase sugarcane at these centres and payment for the cane to the Sugar cane cultivators was required to be made within a fortnight of the date of weighment. The assessee company was required to exhibit on the notice board at each weighment centre the dates and hours at which payments would be made from time to time. In compliance with the statutory rules the assessee company announced that payments to the sugarcane cultivators would be made at Dooria which was one of the purchasing centres on Tuesdays and Sundays of each week. On 16-4-1950, the assessee company deputed one of its employees to go to Dooria and sent a sum of Rs.35,000/- in cash through its employees in a jeep car. The amount of Rs.35,000/- was robbed on the way, and in spite of police investigation the amount was not recovered and the miscreants could not be traced. The amount of Rs.35,000/- was thus debited by the assessee to the cane expenses account as revenue expenditure. The Income-tax officer however, held that the money was not stock-in-trade of the assessee and the deduction cannot be allowed. The assessee company took the matter in appeal to the Appellate Assistant Commissioner who considered that the loss of money was a loss incidental to the business of the assessee and the claim ought to be allowed. The Appellate Assistant Commissioner observed that the assessee sent out money to various centres for distribution to the cane-growers as one of usual operations without which the cane could not be purchased and profit could not be earned. The Income-tax Department preferred an appeal to the Income-tax Appellate Tribunal which held that the loss could not be deducted from the gross profits of the assessee. The Tribunal found that the loss was incidental to

the business of the assessee, but the Tribunal held that they were bound by the decision of this Court in - *'Mulchand Hiralal v. Commissioner of Income Tax, B. and O[1].',* The Tribunal therefore, dismissed the appeal holding that the loss was not deductible from the gross income of the assessee. In these circumstances the Appellate Income-tax Tribunal has submitted the following question of law for the opinion of the High Court.

> "Whether in the facts and circumstances of this case, the loss of the sum of Rs.35,000/- is deductible in computing the total income of the assessee company."

3. On behalf of the assessee Mr. Dutt put forward the argument that the Income-tax Appellate Tribunal was wrong in holding that the decision of this Court in AIR 1938 Patna 159 was applicable; to this case. The contention of learned Counsel was that the loss of the assessee on account of the theft was a loss closely connected with the business of the assessee and could properly be deducted from the gross profits for the purpose of imposing the tax. Learned Counsel also pointed out that the Appellate Tribunal have themselves come to the conclusion that the loss of the money was incidental to the business carried on by the assessee. On the basis of this finding Counsel made submission that the assessee was entitled as a matter of law to deduct the amount of Rs.35,000/-for computation of the total income for the purpose of income-tax. In our opinion, the argument addressed on behalf of the assessee is well founded and must be accepted as correct. It is clear in this case that the purchase of Sugarcane was controlled by statutory rules framed under the Bihar Sugar Factories Control Act. By virtue of these rules the assessee company was bound to set up purchasing centres and to locate weigh bridges for the purchase of sugarcane. The assessee company was also bound to purchase sugarcane at these weighment centres and to make payment to the sugarcane cultivators within a fortnight of the date of weighment. The assessee company was also required to exhibit on the notice board at each weighment centres the dates and hours on which payment would be made from time to time. The relevant rules are Rules 351 36, 41, and 43, Bihar Sugar Factories Control Rules framed under the Bihar Act 7 of 1937. Rule 43, provides that a person who fails to comply with or contravenes any of the rules will be liable to be prosecuted in a Criminal Court. It is manifest, therefore, that the assessee company had to despatch money to various purchasing centres for payment to sugarcane cultivators. That was an essential part of the business of the assesses for the sugarcane factory cannot work unless there is a supply of sugarcane. It appears to us that the loss of money in this case is a loss which springs from the statutory necessity of sending money to various purchasing centres, and such a loss is, therefore, incidental to the business carried on by the assessee. To put it differently, the loss of money is a loss-connected with or arising out of the business of the assessee, and should, therefore, be taken into account in calculating the "profits or gains" under Section 10(1), Income-tax Act for the purpose of computing the taxable income. It was argued by Mr. R.J. Bahadur, Standing Counsel for the Income-tax Department, that the case is not covered by Section 10(2)(xv) for the loss by theft cannot be taken to be an expenditure laid out wholly and exclusively for the purpose of business. The argument is no doubt correct, but the argument has not much bearing on the question at issue in this case. For it is settled by high authorities that the deductions expressly mentioned under Section 10(2), Income-tax Act are not exhaustive, and the question of computing the "profits and gains" of a business under Section 10(1) must be approached in a commercial sense. See for example the decision of the Judicial Committee in - *'Commissioner of Income Tax, C.P. and Berar v. Sir S.M. Chitnavis[2]',* In our opinion, the claim of the assessee in the present case falls within the ambit of Section 10(1),

Income-tax Act. The expression "profits and gains" in Section 10(1) must obviously be understood in the commercial sense. That was the view expressed by the House of Lords in - *'The Gresham Life Assurance Society v. Styles[3]',* the Lord Chancellor states:

> "Now to my mind it is very clear what is the intuitus, both from the enactment and from the rules under which the duties are to be ascertained. The thing to be taxed is the amount of profits and gains. The word 'profits' I think is to be understood in its natural and proper sense in a sense which no commercial man would misunderstand. But when once an individual or a company has in that proper sense ascertained what are the profits of his business or his trade, the destination of those profits or the charge which has been made on those profits by previous agreement or otherwise, is perfectly immaterial. The tax is payable upon the profits realized and the meaning to my mind is rendered plain by the words payable out of profits."

The principle was of course laid down with reference to English law on the point. But in - *'Pondicherry Rly. Co. v. Commissioner of Income Tax, Madras[4]',* it was held by the Judicial Committee that the principle laid down by Lord Chancellor in Style's case was General application and that the principle was unaffected by the specialities of the English tax system. Lord Herschell also observed in - *'Russell v. Town and County Bank[5]',*

> "The profits of a trade or business is the surplus by which the receipts from trade or business exceeded the expenditure necessary for the purpose of earning those receipts."

Unless and until you have ascertained that there is such a balance nothing exists to which the name of profits can properly be applied, Lord Parkar made a similar statement in - *'Ushar's Wiltshire Brewery v. Bruce[6]',* (F):

> "Where a deduction is proper and necessary to be made in order to ascertain the balance of profits and gains, it ought to be allowed, provided there is no prohibition against such an allowance."

In our opinion, Section 10(1), Income-tax Act must be construed in the light of this general principle. In view of our finding that the loss of money by theft was a loss closely incidental to the business of the assessee, we hold that the assessee company is entitled to deduct the sum of Rs.35,000/- in computing its taxable income.

4. Mr. R.J. Bahadur on behalf of the Income-tax Department strongly relied upon the decision of this Court in AIR 1938 Patna 159. The assessee in that case claimed that a sum of Rs.2,960/- which was stolen by a cooly while the money was sent to a bank, should be deducted from the gross profits of the assessee for the purpose of assessment to income-tax. It has held by Courtney Terrell, C.J. in the first place that the loss of money by theft did not occur in the accounting year 1931-32, but occurred in the accounting year 1932-33, and that this

circumstance was fatal to the contention of the assessee. The Chief Justice proceeded to observe that loss by theft was not expressly mentioned as one of the allowances, mentioned in Section 10(2), Income-tax Act. The Chief Justice, therefore, considered that the amount could not be deducted from the taxable income of the assessee. In our opinion the case is not an authority for the proposition that loss by theft cannot in any case be a permissible deduction from the gross profit of the assessee. The observation of the Chief Justice is an obiter dictum and the actual decision of the case can be supported on the finding that loss by theft occurred in the accounting year 1932-1933 and did not occur in the accounting year 1931-32. The decision is also not authoritative because the learned Chief Justice did not take into consideration the provisions of Section 10(1), Income-tax Act. We do not, therefore, think that the decision of the Bench in AIR 1938 Patna 159 is an authority which should govern the decision of the present case. We prefer, on the contrary to support our view by the decision of a Division Bench consisting of Ross and Kulwant Sahay, JJ. in - *'Jagarnath Therani v. Commissioner of Income Tax, B. and O*[7]*.',* This decision had been criticised by Sir Courtney Terrell C. J. in AIR 1938 Patna 159. But, in our opinion, the authority of AIR 1925 Patna 408 has not been shaken in any way by the decision of the Division Bench in AIR 1938 Patna 159. In AIR 1925 Patna 408 the assessee claimed to deduct from his business profits a certain sum of money which was embezzled by the gomashta of the assessee in the ordinary course of business. It was held by the Bench that the loss was allowable as it was a loss incidental to the conduct of the business. The principle of this decision applies to the present case.

5. On behalf of the Income-tax Department Mr. R.J. Bahadur strongly relied upon a decision of the Madras High Court in - *'Ramaswami Chettiar v. Commissioner of Income Tax, Madras(Supra)',* But that case is not really in point for the finding of the majority of the learned Judges was that the loss by theft was not incidental to business. Reference was also made by learned. Counsel for the Income-tax Department to - 'In re L.N. Gadadia and Co.', 1934-2 ITR 322 (Lah) (I). The authority of this case is not of much assistance to the income-tax Department because the finding was that the assessee made a false allegation that he carried on money lending and banking business.

6. It was also found that the loss of money was not a loss of stock-in-trade, but a loss of capital. The decision of this case has also been doubted by the Rangoon High Court in - *'Commissioner of Income Tax, Burma v. Abdul Ganny*[8]*',* Mr. R.J. Bahadur also referred to an Orissa case - *'Bansidhar v. Commissioner of Income Tax, B. and O*[9]*.',*
But the loss wasnot allowed in that case because the High Court agreed with the Tribunal that the loss of money by theft was not incidental to the business nor could, it be held to be loss of stock-in-trade and could not therefore, be allowed as a trading loss. For the reasons we have expressed, we hold that the amount of Rs.35,000/- should be deducted from the total income of the assessee for the purpose of income-tax and the question referred to the High Court must be answered in favour of the assessee and against the Income-tax Department. The Income-tax Department must pay the cost of the reference hearing fee Rs.250/-.
Reference answered.

Cases Referred.

[1] AIR 1938 Pat 159
[2] AIR 1932 PC 178

[3]1892 AC 309. At p.315
[4]5 ITC 363 (PC)
[5](1888) 13 AC 418
[6]1915 AC 433 at p.458
[7] AIR 1925 Pat 408
[8] AIR 1941 Ran185 (SB)
[9] AIR 1952 Ori 109