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Court : Mumbai

Decided On : Oct-09-1939

Reported in : [1940]8ITR7(Bom)

Appeal No. : Income-tax Reference No. 5 of 1939

Appellant : David Sassoon and Co., Ltd., in Re.

Judgement :

Beaumont, C.J. - This is a reference made by the Commissioner of Income-tax under Section 66(2) of the Act. The assessee company were assessed for the financial year 1937-38 in respect of their income of the 'previous year', which expired on the 31st December 1936. During that year they made on the whole a substantial profit, but in respect of the working of the New Union Mills, which formed part of their business during the previous year, they incurred a loss of Rs. 77,236. On the 1st January 1937, the New Union Mills were assigned to a Company called the New Union Mills, Ltd., which was a new Company formed for working the mills. The Income-tax Officer refused to allow the assesseees to set off their loss of Rs. 77,236 under Section 26 of the Income-tax Act, because he held that by virtue of Section 26(2) of the Act the assesseees were not assessable in respect of the New Union Mills. In point of fact the assessee were not liable for any tax in any event, because they had accumulations of depreciation arising under section 10(2) (vi), proviso (b) which wiped out the tax which would otherwise have been payable. The question is whether or not this loss of Rs. 77,236 can be deducted from accumulation of depreciation.

Now the question to my mind turns on the construction of Section 26(2) of the Act, which provides :-

'Where at the time of making an assessment under Section 23, it is found that the person carrying on any business, profession or vocation has been succeeded in such capacity by another person, the assessment shall be made on such person succeeding as if he had been carrying on the business, profession or vocation throughout the previous year, and as if he had received the whole of the profit for that year.'

The meaning of that section seems to me to be plain. If at the time of the assessment the Income-tax Officer finds that there has been a succession to a particular business, then it is the successor who must be assessed, and the predecessor cannot be assessed. The successor is to be assessed on the basis of two hypotheses. First, that he had been carrying on the business for the whole of the previous year, and secondly, that he had received the whole of the profits for that year. Those hypotheses, in my opinion, can only be applied if and so far as the facts permit. It may be that the business assigned came into existence only during the previous year, in which case the assessee cannot have been carrying it on during the whole of the previous year since it did not exist for that period, and it may be that there were no profits in which case the assessee cannot have received the profit. But the fact that those two hypotheses on which the assessment has to be based do not exist, in my opinion, in no way, affects the peremptory words of the Act which require that where there has been a succession to a business it is the successor, and not the predecessor, who is to be assessed. If that is the meaning of Section 26(2), then Section 24 which enables an assessee to set off the loss of profits under any head mentioned in Section 6, against the profits received under any other head, can only apply in a case falling under Section 26(2) to the successor, who is the only assessee. It was so held by this Court in *Bhogilal Hargovandas Patel v. Commissioner of Income-tax, Bombay* : [1937]5ITR555(Bom) In that case an argument was presented to the Court that Section 26(2) would not apply at all if there were no profits of the business for the previous year. I myself declined to express any opinion on the point, because as I pointed out, on the facts the question did not arise. Mr. Justice Blackwell did

express the opinion that Section 26(2) would apply, although there were no profits.

The assessee relies strongly on a subsequent decision of the Calcutta High Court in *In re B. K. Paul & Co.*, which is reported in : [1938]6ITR395(Cal) In that case the 'previous year' was the year 1932-33. The assignment there in question took place more than a year afterwards, viz., in April, 1934, and the assessment took place in September 1934. The case is therefore distinguishable on the facts and it may well be that an assessee could not be assessed in respect of a business which he acquired more than a year after the termination of the previous year in which the profits were assessed. I am disposed to think that Mr. Justice Khundkar based his decision very largely on that ground, because he says, referring to *Bhogilals* case :-

'It was not established as it has been here, that at the time in question, an order of assessment could not have been passed upon the successors.'

However, Mr. Justice Mukherjea undoubtedly based his judgment on the view that Section 26(2) does not apply where there no profits for the year on which the assessment is based. He thought, as I understand him, that applying the section to such a case would lead to great hardship where, as in the present case, the predecessor has made substantial profits under other heads against which but for the assignment, he could have set off the loss in respect of the business assigned. He thought it was unreasonable to suppose that the Legislature could have intended to deprive the assignor of that right. But as against such consideration must be set the case which might very easily arise because a going concern often acquires a deficit business, of a successor who has made large profits in respect of other heads and has incurred loss, partly actual and partly notional in respect of the particular business acquired. In such a case, if he is not the assessee under Section 26 (2), he must lose the benefit, which he would otherwise have possessed, of setting off his loss against profits under Section 24.

To my mind all that the Court can do is to apply the plain words of Section 26(2), which require that, where you find at the time of assessment there has been a succession you must assess the successor and not the predecessor. Whether by so doing one or the other is deprived of an advantage, which he would otherwise

have enjoyed under Section 24 seems to me irrelevant. Section 24 does not apply by any means to every assessment; it only applies where there is a profit under one head, and a loss under another. With great respect to Mr. Justice Mukherjea, I think that his opinion fails to give effect to the natural meaning of Section 26(2) of the Act, and that it is quite impossible to read that section as conditional on there having been profits of the business, any more than it can be made conditional on the business having existed for the whole of the previous year.

We have been referred to one other case, Gokaldas Lakhmichand v. Commissioner of Income-tax, Bombay, a decision of the Judicial Commissioners Court at Sind, which is reported in 5 I.T.R. 519 That case seems to me inconsistent with the decision of this Court in Bhogilals case, and I think it was wrongly decided.

The first question which is raised is :-

'Whether in the circumstances of this case, Messrs. David Sassoon & Co. Ltd., are entitled to set off under Section 24 of the Income-tax Act or under any other provision thereof the sum of Rs. 77,236 being the loss sustained by them in respect of part of their business carried on by under the name of the Union Mills.'

The answer to that must be in the negative.

The second question raised is -

'Whether in the circumstances of this case, Messrs. David Sassoon & Co., Ltd., are entitled to carry forward the amount of depreciation for the financial year 1936-37 as also the arrears of depreciation for previous years in respect of the machinery, plant, etc., used in connection with the aforesaid business.'

It seems to me plain that on the constriction of Section 10(2) (vi), proviso (b) the right to set off past depreciation only exists in the person who continues to derive profits in respect of the business concerned. I think the answer to the second question is plainly in the negative.

The assessee to pay the costs.

Kania, J. - The relevant facts are stated in the judgment of the learned Chief Justice which is just delivered.

Apart from decided authorities the determination of the question must depend on the true construction of Section 26(2). The section in terms states that when there is succession in business the assessment shall be made on the person succeeding. It is therefore clear that when there is a transfer or succession to a business the assessee is the transferee or the successor. The next question which will arise is on what footing is he to be assessed. That is laid down in the latter part of Section 26(2). It is there provided that he is to be assessed 'as if he had been carrying on business throughout the previous year'. That sets at rest the controversy as to what is to happen when a business is transferred in the middle of a year. Then follow the words which have given rise to a difference of opinion. The words are 'as if he had received the whole of the profits for that year'. One reason for inserting those words in the section is obviously to set at rest the question what is to happen when the predecessor had received in fact part of the profits and the successor had received the rest. The section provides that in that event the successor has to be assessed on the footing that he had received the whole of the profits of the previous year.

The contention urged on behalf of the assessee is that if the intention of the Legislature was to adopt the same method of assessment when there was a loss they would have stated also 'as if the whole loss had been sustained by the successor'. One obvious answer to this argument is that the legislature will not be expected expressly to provide for a case when there was a loss as the result of the years business. The arguments for the assessee however must rest on the decision of the question whether Section 24 has to be read as applicable to the predecessor in spite of Section 26, or Section 26(2) is the governing section when there is an assignment.

Having regard to the fact that Section 26(2) is imperative about who is to be assessee, it is not proper to contend that in respect of the business which is assigned, the producer could be an assessee in any view of the matter. If this aspect is borne in mind, I think, there is no conflict between the two sections.

Section 24, it is urged, could be applicable only to the predecessor because he had sustained the loss. The argument is unsound because the predecessor is not the assessee of the business which was assigned. In order to invoke the application of Section 24 the present assessee (predecessor) must be held to be the same assessee who was being assessed for the business which had been transferred. Section 24 assumes that the assessee is liable to be assessed under the particular head in respect of which he has suffered loss. On transferring the business he has ceased to be an assessee who is liable to be assessed under that head, and Section 24 in terms will not apply to him as regards the business which is assessed.

It was urged on behalf of the assessee that in order to uphold the contention of the income-tax authorities Section 24 will have to be read as including the words 'deemed to have incurred' in favour of the successor. We are not concerned in this case with what rights the successor has to set off the loss. An attempt to go into the motive of the Legislature will land the Court in going beyond the express terms of the Sections. With all respect to the learned Judge who decided *In re B. K. Paul & Co.*, (6 I.T.R. 365), it appears that Mr. Justice Mukherjea was greatly impressed by the motive which led the Legislature to formulate Section 24. I apprehend that is not the correct way to approach the interpretation of the section, when the words of the section are plain and unambiguous.

In *In re B. K. Paul & Co.*, on which the assessees strongly relied the facts were that the assessees, a Hindu undivided family owned real property, securities, shares and 17 business. During the accounting year 1932-33, which ended on 13th April 1933, the assessees received income from real property, securities and shares but there was a loss in business. Assessment proceedings started in 1933-34 but were not completed until 31st March 1934. On 14th April 1934 sixteen out of the seventeen businesses were transferred to four new limited companies. The income-tax authorities came to know of it and when passing the assessment order on 28th September 1934 they refused to allow the assessees to set off the loss incurred in business against their other incomes. The question submitted for the opinion of the Court was : 'Where an assessment proceeding for 1933-34 is started but not completed during that year and during its pendency in the next year

the assessee hitherto carrying on business is succeeded in such capacity by another person whether set off under Section 24 of the Indian Income-tax Act for the loss sustained in that business during the year 1932-33 can be claimed by the assessee or whether such set off will be allowable only to the successor.' The Court answered the question in the affirmative as regards the assessee.

The facts clearly show that the case could not be covered by Section 26(2). For the year 1933-34 the Hindu family firm was being assessed, on its income for 1932-33 in which year they had carried on business. In the accounting year 1933-34 for which the income of the previous year, i.e., 1932-33 will be the basis, the limited companies were not in existence. Under the words of Section 26(2) in that case the accounting year was 1933-34 and the 'previous year' was 1932-33. The limited companies were not liable to be assessed for that accounting year at all. In respect of the business, if any, conducted by the Hindu family for the year 1933-34, when the limited companies were called upon to furnish their return in respect of the accounting year 1934-35, what the position would be is not at all found in the judgment. I do not see how it could have been urged that the case was covered by Section 26(2) under the circumstances of that particular case. The 'previous year' is the year before the 'accounting year' and as the first accounting year in which the limited companies could have been assessed was 1934-35 the previous year must be 1933-34. In the course of his judgment Derbyshire, C.J., has stated as follows :-

'It is true that in the accounting year next but one following, the four new companies which has no existence during the accounting year ending April 13, 1933, succeeded to the sixteen business. Yet it cannot be said that these four companies sustained a loss in the year ending April 13, 1933; they were not in existence in that year and were neither making gains for sustaining losses. Cases may arise in which there will be a conflict as to the right to the set off as between the transferor and the transferee of a business which has suffered losses during the accounting year. The terms and circumstances of the transfer may indicate whether there has been a succession within Section 26(2) and what the rights of the respective parties are in such cases. No such conflict arises here in my opinion and I do not propose to anticipate it.'

It must be conceded that the Court did consider the applicability of Section 26(2) when there was a loss only but under the circumstances the statements found in the judgment are all mere expressions of opinion which were not necessary for the determination of the question before the Court. The terms of the question put to the Court clearly indicate the question was deliberately framed on the special facts of that case and was not a general question.

Having regard to the clear words of Section 26(2) and for the reason that there cannot be two assesseees in respect of the same business the contention of the Taxing authorities should be upheld in this case.

On second question I think that the answer should be as stated by the learned Chief Justice. The right to claim depreciation is not a personal right of the party who has parted with the ownership of the property in respect of which depreciation is to be assumed.

The Order of the Court was as follows :-

ORDER

Upon the Reference of the Commissioner of Income-tax for the Bombay Presidency, Sind and Baluchistan dated the tenth day of July one thousand nine hundred and thirty nine arising out of the order of the Assistant Commissioner of Income-tax, Bench Division, Bombay, in the above matter dated the ninth day of August one thousand nine hundred and thirty eight in appeal on the grounds mentioned in the Petition herein dated the nineteenth day of September on for hearing on the sixth day of October instant and this day the said Commissioner and the above named assesseees Messrs. David Sassoon and Company Limited appearing respectively by Advocates and upon reading the said Reference and the Order passed on the ninth day of August one thousand nine hundred and thirty eight by the Assistant Commissioner of Income-tax, Bench Division, Bombay this court both answer the questions referred to in the said Reference in the negative and both declare that the Assesseees, Messrs. David Sassoon and Company Limited are not entitled to set off under Section 24 of the Income-tax Act or under any other provision thereof the sum of Rupees seventy seven thousand two

hundred and thirty six being the loose sustained by them in respect of part of their business carried on by them under the name of Union Mills and this court both further declare that the said Assesseees are not entitled to carry forward the amount of depreciation for the financial year 1936-37 as also the arrears of depreciation for previous years in respect of the machinery, plant and other things used in connection with the aforesaid business and this court both order that the said Assesseees do pay to the said Commissioner his costs of the said Reference and of this Order when taxed on the original side scale and noted in the margin thereof. Witness Sir John William Fisher Beaumont, Knight Chief Justice at Bombay aforesaid this ninth day of October one thousand nine hundred and thirty nine.

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