(1958) 09 BOM CK 0025

Bombay High Court

Case No: Income Tax Reference No. 86 of 1957

Indore Malwa United Mills Ltd.		APPELLANT
	Vs	
Commissioner of Income Tax (Central), Bombay		RESPONDENT

Date of Decision: Sept. 23, 1958

Acts Referred:

- Income Tax Act, 1922 - Section 10(2), 24(2)

Citation: (1959) 35 ITR 271

Hon'ble Judges: Chagla, C.J; S.T. Desai, J

Bench: Division Bench

Advocate: R.J. Kolah, for the Appellant; G.N. Joshi, for the Respondent

Judgement

Chagla, C.J.

This reference raises two questions, and the facts which have got to be stated in order to answer those two questions are these. The assessee company mainly carried on its business in Indore and it is an admitted fact that in the year 1948-49 it made a loss of Rs. 5,19,590. The assessee company was assessed to tax in that year in India. It is also not disputed that under the tax laws prevailing in Indore and which were applicable to the assessee company, this particular loss could not be carried forward. In the years 1948-49 and 1949-50 depreciation was allowed to this company in the sum of Rs. 2,00,705 and Rs. 3,37,025. These amounts could not be absorbed because the company had incurred losses or there were not sufficient profits to absorb this depreciation which was allowed. In the assessment year 1950-51 two claims were made by the company. One was with regard to this loss of Rs. 5,19,590 and the assessee company''s contention was that it was entitled to set off this loss against the profits made in its business in that year, and it also contended that it was entitled to carry forward the unabsorbed depreciation into this year. The first contention of the assessee company was rejected by the Tribunal; the second was allowed; and two questions have been raised, one at the instance of

the assessee company and the other at the instance of the Commissioner, dealing with these two aspects of the matter.

2. Turning to the first question, the difficulty is caused by the fact that in 1948-49 we had the Indian State of Indore and certain provisions applied under the Indian Income Tax Act to the profits earned in an Indian State. When we come to 1950-51, which is the year of assessment, the complications both political, economical and financial caused by the existence of Indian States have been done away with and we have one State to which the Income Tax Act applies without any difference or distinction, and what we have to decide in this case is how the two different situations have got to be reconciled. What is urged by Mr. Kolah on behalf of the assessee company is - look at the Income Tax Act, 1950-51 that is the law to which the assessee company is subject, and if that law permits the assessee company to set off this loss of Rs. 5,19,590 then it is no answer to say that the position might have been different in 1948-49. Let us turn to the relevant provisions with regard to set-off. We have first section 24 (1) and that deals with a set-off with regard to a loss under one head being set-off against profits under other heads. To this section there is a proviso and the effect of that proviso is - to translate that proviso into simple language - that if a loss has been made in an Indian State, that loss cannot be set off against any other head except the profits made in the Indian State itself. The reason for this proviso is obvious. Under the law as it stood in 1948-49, profits made in an Indian State were not subject to tax except when they were brought into what was then known as British India. Therefore, when an assessee was assessed in British India he was not liable to pay tax on the profits he might have made by carrying on a business in an Indian State. If he brought those profits into British India then he had to pay tax. But if he kept the profits in the Indian State then they were exempt from tax; those profits were considered to be exempted from tax or profits which were not liable to tax. Now, having exempted those profits from tax, it stood to reason that when losses were made the assessee could not take the benefit of the set-off with regard to those losses. Therefore, the proviso to section 24 (1) laid down that an assessee could only claim to set off his losses incurred in an Indian State against the profits also earned in the Indian State. Coming to section 24 (2), that gave an additional right to an assessee and that right was that if the losses incurred in a business could not be set off against the profits under any other heads and some loss still remained which was not set off, the assessee had the right to carry forward that loss and to set off the same within six years against the profits earned in the same business. To this section also there was a proviso and that proviso corresponded to the proviso to section 24 (1) and the proviso was :

"Where the loss sustained is a loss of profits and gains of a business, profession or vocation to which the first proviso to sub-section (1) is applicable, and the profits and gains of that business, profession or vocation are, under the provisions of clause (c) of sub-section (2) of section 14, exempt from tax, such loss shall not be set off except against profits and gins accruing or arising in an Indian State from the

same business, profession or vocation and exempt from tax under the said provisions."

3. Just as he could not set off against any other head u/s 24 (1), similarly u/s 24 (2) where we are dealing with exempted losses, he could only carry forward and set off against exempted profits.

4. Now, the whole of Mr. Kolah''s argument is that in 1950-51 the assessee company has made profits which are liable to tax. He had incurred losses in 1948-49 and u/s 24 (2) there is a mandatory provision that those losses shall be carried forward. He says that it is not for him to carry those losses forward, it is not for him to make any claim; it is the statutory obligation of the Department that these losses shall be carried forward; and if he is in a position to satisfy the Department that there are profits made in the same business in which the losses were incurred, he is entitled to set off those losses against the profits of that business. The argument on the face of it seems very plausible. But the fallacy in the argument is this that before you come to section 24 (2), before you can claim to carry forward losses, the losses must be such as could have been set off initially u/s 24 (1) ,because section 24 (2) says "and the loss cannot be wholly set off under sub-section (1), the portion not so set off shall be carried forward." Therefore, not only they have not been set off in fact u/s 24 (1) but they could not have been set off u/s 24 (1). Admittedly, these losses could not have been set off u/s 24 (1) because of the proviso in 1948-49. If they could not have been set off, no right to carry forward u/s 24 (2) can arise. In our opinion, the condition precedent to the application of section 24 (2) is that the losses in respect of which a special right is given to carry forward for six years must be losses to which initially section 24 (1) must apply. If they are losses to which section 24 (1) does not apply and they are not losses which could have been set off against any other head, no question of carrying forward u/s 24 (2) can arise, and that is exactly the position here. On the face of it, the claim made by the assessee company is untenable. It could not have claimed to set off these losses against any other head u/s 24 (1) and in fact it did not. When we come to the year 1950-51, it says - "Well I could not have set off these losses against any other heads in 1948-49, but u/s 24 (2) I am entitled to carry forward these losses up to six years, only two years have elapsed, and there is nothing in section 24 (2) to prevent me from making this claim." The answer is - what is there to prevent it from making this claim is the absence of the very condition u/s 24 (1) which permits an assessee to carry forward the losses u/s 24 (2) and that condition is that these losses must be such losses as could have been set off u/s 24 (1). If they could not have set off at all, no question of carrying them forward u/s 24 (2) arises. Therefore, in our opinion, the Tribunal was right in the conclusion it arrived at.

5. There is further support to this argument in the provision made in the Removal of Difficulties Order, 1950. Under clause 3 it was provided :

"Where in any previous year prior to the previous year for the assessment for the year ending on the 31st day of March, 1950, an assessee has sustained a loss of profits or gains in any business, profession or vocation carried on by him, and such loss would, had the State law continued to be in force, have been set off against the profits and gains, if any, from the same business chargeable to tax in the said year of assessment or in any year subsequent thereto, such loss would be so set off in the same manner, to the same extent, and up to the same year of assessment, as it would have been set off had the State law continued to be in force."

6. So clause 3 gives a right to the assessee to avail himself of the provisions of section 24 (2) provided the law of the Indian State permitted him to carry it forward. As we have pointed out, in this case the law of the Indore State did not permit the assessee to carry forward the loss. Therefore, Mr. Kolah himself concedes that his case does not fall under clause 3, but what he days is that although it does not fall under clause 3 it falls under the ordinary law. Well, the argument is not conclusive, but undoubtedly it helps us in the interpretation of the Income Tax Act that the Government realised that considerable hardship would be caused to the assessee who had the right of carrying forward the losses in their own State, and, therefore, that particular right was continued when integration came into force. But what Mr. Kolah claims is something much more that although he could not have availed himself of this right if there had been no integration and under the Indore law he could never have carried forward the losses, still by reason of the integration this new right of carrying forward the losses was available to him. Now, the only right integration has given to an assessee is the right contained in clause 3 of the Removal of Difficulties Order, 1950, and that right is that if the law of his own State permitted him to carry forward the losses, then that right is preserved under the Indian Income Tax Act.

7. The other question presents much less difficulty. As already pointed out, under the rules of taxation which prevailed in Indore, the assessee was entitled to carry forward depreciation in the years 1948-49 and 1949-50 which could not be absorbed, and the question that now arises is whether he could rely on these amounts for the purpose of aggregate depreciation in the relevant assessment years. The provision that calls for our consideration is clause 2 of the Taxation Laws (Part B States) (Removal of Difficulties) Order, 1950, and that clause provides :

"In making any assessment under the Indian Income Tax Act, 1922, all depreciation actually allowed under any laws or rules of a Part B State relating to Income Tax and super-tax, or any law relating to tax on profits of business, shall be taken into account in computing the aggregate depreciation allowance referred to in sub-clause (c) of the proviso to clause (vi) of sub-section (2) and the written down value under clause (b) of sub-section (5) of section 10 of the said Act."

8. Now, what is urged by the Department is that this provision only permits the assessee to take into account the depreciation allowed under the Indore laws for a

specific purpose of sub-clause (c) of the proviso to clause (vi) of sub-section (2) of section 10 and for the purpose of ascertaining the written down value under clause (b) of sub-section (5) of section 10. It is urged that the question that we have now to consider does not fall under sub-clause (c) of the proviso to clause (vi) of section 10 (2), but it falls under sub-clause (b) of the proviso, and as there is no reference to sub-clause (b), the assessee is not entitled to the benefit which that sub-section provides for the assessee. In our opinion, this contention is based on a misapprehension of the scheme embodied in clause 2 of the Removal of Difficulties Order, 1950.

9. When we look at the relevant provisions of the Act, section 10 (2) (vi) lays down the allowances to which an assessee is entitled in respect of profits and gains of his business for depreciation and the clause contains the various indications as to how the depreciation is to be calculated. There is a proviso to sub-section and sub-clause (b) of the proviso provides for carrying forward of depreciation which has been allowed when that depreciation cannot be absorbed by reason of profits and gains being sufficient for that purpose, and sub-clause (c) is in the following words :

"(c) the aggregate of all such allowances made under this Act or any Act repealed hereby, or under the Indian Income Tax Act, 1886, (II of 1886) shall, in no case, exceed the original cost to the assessee of the buildings, machinery, plant or furniture as the case may be."

10. Therefore, in a sense sub-clause (c) lays down the ceiling of the depreciation which can be allowed. But in order to ascertain that ceiling the aggregate of such allowances has got to be taken into consideration, and such allowances would include an allowance permissible under sub-clause (b). Therefore, in order to ascertain the aggregate the allowances permissible under sub-clause (b) must be taken into account and into consideration, and therefore when clause 2 of the Order refers to sub-clause (c) it does not confine the operation of that clause to that sub-clause because it only refers to sub-clause (c) and it refers to sub-clause (c) for the purpose of indicating how the aggregate depreciation is to be calculated. Therefore, in our opinion, the very application of sub-clause (c) necessarily requires the application of sub-clause (b), and therefore it is untenable to contend that in determining the aggregate under sub-clause (c) it is not permissible to the assessee to carry forward the depreciation which is permissible under sub-clause (b). There is a further clear indication that the view we are taking is correct in the explanation to clause 2 of the Order which was subsequently substituted and that explanation is :

"For the purposes of this paragraph, the expression ''all depreciation actually allowed under any laws or rules of a Part B State'', means and shall be deemed always to have meant the aggregate allowances for depreciation taken into account in computing the written down value under any laws or rules of a Part B State or carried forward under the said laws or rules."

11. Now, this explanation makes it amply clear that in determining the aggregate, depreciation which can be carried forward under any rules applicable to a Part B State must also be taken into account. In our opinion, the Tribunal was right in the view that it took on both the questions.

12. The result therefore is that the answer that we must give to question (1) is in the negative and the answer to question (2) in the affirmative.

13. No order as to costs.

14. Questions answered accordingly.