# Rajputana Trading Co. Ltd. vs Commissioner Of Income-Tax, West ... on 5 September, 1968

## Equivalent citations: AIR1969SC572, [1969]72ITR286(SC), (1982)2SCC775, [1969]1SCR1013, AIR 1969 SUPREME COURT 572

## Bench: A.N. Grover, J.C. Shah, V. Ramaswami

JUDGMENT

Grover, J.

1. This is an appeal by certificate from a judgment of the Calcutta High Court answering the following question referred to it in the negative and against the assessee :

> "Whether, on the facts and in the circumstances of the case, the sum of Rs. 78,749, which was deemed to be the profits and gains of business under section 10(2A) of the Income-tax Act, can be said to be arising from speculative business ?"

2. The assessee carried on both speculative as well as non-speculative business. The system of account regularly employed being mercantile, any liability for payment of difference on account of speculative transactions is allowed as a deduction in computing the profit or loss in speculative business. At the commencement of the accounting year relevant for the assessment year 1955-56, i.e., July 1, 1953, there was a balance of such liabilities for speculation differences in the account of one Ramnath Narendranath amounting to Rs. 83,049. Out of this liability the assessee had paid to the party a sum of Rs. 7,825 in cash. The balance of Rs. 75,224 along with a sum of Rs. 3,525 being similar liability due to other two creditors aggregating Rs. 78,749 was written back and taken credit of in the profit and loss account for the year ending June 30, 1954. The creditors had waived their right to receive the amount. The Income-tax Officer treated the amount was of Rs. 78,749 as the assessee's income from business in terms of section 10(2A) of the Income-tax Act, 1922, hereinafter called the Act. The amount was not set off against the speculative loss either brought forward from the earlier years or suffered by the assessee during the accounting period on the ground that the liability written back and treated as business profit did not partake of the character of speculation profits.

3. The contention of the assessee was that the amount should be treated as profit speculative business as the liability which was written back related to such business. In other words, the assessee claimed that the amount of Rs. 78,749 should be available for set off against speculation loss. the revenue authorities did not accede to this contention. Before the Tribunal it was pressed on

behalf of thee assessee that the department could not stop by treating the liability written back as income from business but must also categories and specifically describe what the nature of the business was and, since the liability related to the particular business, the income could only only be construed as arising from that business. The Tribunal negatived this contention. According to it the effect of the provision of section 10(2A) of the Act is that it charges the amount to tax by its own force as a business income. "The income character if the receipt is designated by the fiction of law and it is to be brought under assessment as an income from business without any further categorisation. It cannot, therefore, be said that this income arose to the assessee from any speculation business. It is treated as business income only by virtue of the specific provision made in this regard".

4. The High Court referred to the decision of this court in Donald Mira nda v. Commissioner of Income-tax , but held that there was no warrant for saying that the remission of a speculative liability should be treated as speculative income accruing to the assessee. The decision of this court was distinguished on the ground that it related to refund of excess profits tax which stood on a different footing inasmuch as it had to be laid because of an unusual rise in the income of the assessee over the standard profits and when refund of the tax paid was made it was logical to hold the same as income from business in respect of which the excess profits tax liability arose.

5. Section 10(2A) of the Act was in these terms :

> "Where for the purpose of computing profits or gains under this section, an allowance or deduction has been made in the assessment for any year in respect of any loss, expenditure or trading liability incurred by the assessee and, subsequently during any previous year, the assessee has received, whether is cash or in any other manner whatsoever, any amount is respect of such loss or expenditure or has obtained some benefit in respect of such trading liability by way of remission or cessation thereof, the amount received by him or the value of the benefit accruing to him shall be deemed to be profits and gains of business, profession or vocation and to have accrued or arisen during that provision year".

6. It is apparent that one of the main purpose of the above provision which has been now re-enacted with some changes in section 41 of the Income-tax Act, 1962, was to catch cases of remission of debt by creditors in respect of earlier trading items which were allowed as deduction. As pointed out by the High Court, in the present case,if a portion of the loss or liability incurred by the assessee in a particular year is subsequently diminished by way of remission or otherwise, section 10(2A) creates a fiction and directs that the remission or the diminution shall be deemed to be profits and gains of business, profession or vocation and to have accrued or arisen during the relevant previous year. The contention of the assessee, however, was that the fiction should be carried a step further and if the loss in respect of which the portion was remitted was a speculative loss the notional profits and gains of business which came into existence by the fiction of the section should be categorised as speculative income. Now it is difficult to understand how the fiction should not be carried to its logical conclusion by necessary implication. When the loss or the liability for which deduction had previously been allowed to the assessee arose out of speculative transactions the origin of such loss

or liability is known and ascertainable. If such loss or liability is to be treated as profits in the circumstances given in section 10(2A) it would be most illogical and irrational to treat the so-called profits as having a neutral source and not springing out of the same category of speculative business which led to the assessee incurring that loss or liability. The decision of this court in Donald Miranda's case , may not be directly in point but there are certain observations in it which are quite apposite. It has been held therein that, when any portion of the tax collected on excess profits is refunded under the provisions of the Indian Finance Act, 1942, or the Excess Profits Tax Ordinance, 1943, it necessarily has the same quality which it had before the amount, which was charged with the payment of the tax, had under the provisions of those Acts. This is what was observed at page 170 :

7. "It would thus appear that the amount of excess profits tax was an allowable deduction for the purpose of computation of the business profits of an assessee under section 12(1) of the Excess Profits Tax Act and when it or a portion of it was refunded it had to be treated as income of the assessee. When it was deposited with the Central Government it was a portion of the profits of the business of the assessee and when it was returned to the assessee it must be restored to its character of be ing a part of the profits of a business. It cannot be said that its nature changes merely because it is refunded as a consequence of some provisions in the Finance Act or the Excess Profits Tax Ordinance. Its nature remains the same. The effect of the deposit under the Acts above mentioned was as if a slice o of the business profit was taken and deposited with the Central Government Treasury and then when it was found that a larger amount had been deposited than was exigible a portion of it was returned. By being put in a Government Treasury it does not cease to be what it was before, i.e., profits of a business."

8. Keeping in view the entire process by which remission of liability is to be deemed to be profits and gains of business, ect., within the meaning of section 10(2A), it is difficult to understand how such profits and gains can be completely divorced from the speculative business in respect of which allowance was made in the earlier year. That allowance or deduction was not liable to be reopened except for the reason that the creditors waived the payment of the debts to them by the assessee which attracted the fiction introduced by section 10(2A) of the Act. According to the counsel for the assessee full effect must be given to that fiction and if full effect is given the conclusion is inevitable that the income in question is income from speculative business. Thus, there is no question of resorting to any double fiction. The simplest and the most obvious way of looking at the at matter is that once the amount of liability which is written back is to be treated as income from business it must be categorised and related to some bussiness. In cases of the present kind there is a fairly direct and proximate relationship between the income as deemed to be arising under section 10(2A) and the speculative business which the assessee was carrying on. This income could not and would not have arisen but for the fact that in the speculative business the assessee had claimed deductions on account of liabilities for speculation differences.

9. There is a good deal of force in the point of view pressed on behalf of the appellant that under the provisions of section 24 of the Act the profit or loss which is computed has to be categorised as either speculative profit or loss or non-speculative profit or loss. If once a particular item of loss is categorized as speculative loss then, in that case if such loss is to be deemed to be income or profit

from the business, profession or vocation by virtue of the provisions of section 10(2A) it follows by necessary implication that such income or profit can only be income or profit arising from speculative business. Moreover, section 10(2A) envisaged that the deemed income which is sought to be taxed should be considered to have arisen from the same business in which the loss that had been incurred was written back. It would be highly p problematical to say that the deemed income arises from a non-descript business when the nature of the business which had given rise to the liability originally is known.

10. The above submission of the appellant effectively meets the main reasoning which prevailed with the High Court that when section 10(2A) treats the remission of liability as profits of the assessee's business, profession or vocations without giving to it any "local habitation or name", there is no reasons why it should be treated as profits and gains of the same kind of business in which the liability was incurred.

11. In our opinion, the question which was referred to the High Court should have been answered in the affirmative and in favour of the assessee. The appeal is accordingly allowed and the answer returned by the High Court is hereby discharged. In view of the nature of the point involved the parties are left to hear their own costs.

12. Appeal allowed.