S.P.S. Ramaswami Chettiar And Ors. vs The Commissioner Of Income-Tax on 1 May, 1930

Equivalent citations: (1930)59MLJ403

JUDGMENT

Horace Owen Compton Beasley, C.J.

1. The facts in this case have been sufficiently set out in the answers to the question referred to us of my learned brothers Anantakrishna Aiyar and Curgenven, JJ., which I have had the advantage of seeing and I therefore do not propose to state them. The question seems to me to resolve itself into one as to whether the loss sustained by the assessee in this case was one which can be described as incidental to his business. If it was, then he is entitled to have his profits upon which he is liable to pay income-tax reduced by the amount of that loss. It was argued for the assessee (1) that the robbery of the assessee's money was one which was incidental to his business of a money-lender,, and (2) that the money stolen was his "stock-in-trade," because it was money which, had it not been stolen, was available to him for the purpose of lending to borrowers and making a profit thereby. There is no evidence in this case that this sum was "stock-in-trade' ' at all and the money would seem to me to be capital plus the profits collected by the assessee. If this money was capital, then the assessee would not be entitled to a deduction on account of its loss. So far as the money stolen was the profit of the assessee, unless it can be shown that its loss was incidental to the business he carried on, he cannot claim a deduction in respect of it. If any one is paid a sum due to him as profits and he puts that in his pocket and on his way home is robbed of it, it would be, I think, difficult to contend that such a loss was incidental to his business. Still more so when he has reached his home and put those profits in a strong room or some other place regarded by him to be a place of safety. I can well understand that in cases where the collection of profits or payment of debts due is entrusted to a gumastah or servant for collection and that person runs away with the money or otherwise improperly deals with it, the assessee should be allowed a deduction because such a loss as that would be incidental to his business. He has to employ servants for the purpose of collecting sums of money due to him and there is the risk that such servant, may prove to be dishonest and instead of paying the profits over to him convert them to his own use. But I cannot distinguish the present case from the case of any professional man or trader who, having collected his profits, is subsequently robbed of them by a stranger to his business. In this case none of the thieves were the then servants of the assessee although one of them had formerly been his cook. This is no doubt a very hard case and, whilst I have every sympathy with the assessee, I am unable to answer the question except in the negative. The question referred to us is rather too general but upon the facts of this case which, in my opinion, are not at all adequately set out, that must be my answer.

2. The result is that the answer of this Full Bench is in the negative and the assessee is directed to pay the costs of the Income-tax Commissioner which we fix at Rs. 250.

Anantakrishna Aiyar, J.

3. I have the misfortune in this case to differ from the opinion of my Lord the learned Chief Justice, and of my learned brother Curgenven, J.

4. The question referred for our decision under Section 66 of the Indian Income-tax Act is "Whether the loss incurred by theft of money used in the money-lending business, and.in the business premises should be allowed for in computing the income-tax."

5. The question raised is one of very great importance, and the case is one of first impression, no case directly deciding the point having been brought to our attention.

6. One should have liked that more facts were available; the facts, as they appear in the records before us, are the following:

> The petitioners are a registered firm of Nattukottai Chetties carrying on money-lending business at Karaikudi and other places in British India, and at Kuala Lampur in Federated Malay States, the headquarters being at Karaikudi in the Ramnad District. On the night of the 21st October, 1926, certain persons broke into the strong room of the house at Moulmein-gyun (Burma) occupied by the petitioners and by two other firms, and stole cash and currency notes of the value of Rs. 9,335 besides certain jewels which had been pledged with the firm, as security, by certain customers. On 5th August, 1927, four persons were convicted of the said offence by the Magistrate. One of these persons had been employed as a cook at the above-mentioned premises. Though he was not so employed at the time of the offence, he was convicted, in addition, under Section 328, Indian Penal Code, of administering drugs to the inmates of the house to facilitate the commission of the theft. The Commissioner of Income-tax stated that he had since the decision of the Income-tax Officer ascertained that the loss of the cash and the jewels was genuine. He, however, was of opinion that there was no provision of law under which the assessees would be entitled to deduction claimed in respect of the cash and currency notes, that the loss could neither be said to be a business loss nor expenditure incurred for earning profits; and that the loss in question is loss of capital. The decision in Jagarnath Therani v. Commissioner of Income-tax, Bihar,and Orissa (1925) 2 I.T.C. 4 was distinguished on the ground that the loss in the present case could not be said to have been incurred in the business at all, and that such a loss could not be said to have been incurred solely for the purpose of earning the profits and gains of the business. He, therefore, held that the loss due to theft committed by persons unconnected with the business is not allowable as a deduction.

7. The learned Counsel who appeared in support of the assessment argued that the allowance now claimed could not be brought under any one of the clauses of Section 10 of the Act, which, he argued, exhausted the headings under which allowances could be claimed by assessees. I am unable to accede to that contention. Section 10, no doubt, directs that the allowances mentioned in the

section should be made in favour of the assessee; but in my view it does not necessarily follow that the assessee is not entitled to the allowance now in question simply because it is not specifically mentioned in Section 10. Under Clause 1 of Section 10, tax is payable only in respect of the profits or gains of any business carried on by the assessee. The Court has to find out what the profits or gains of the business ' amounted to. In the absence of any specific provisions in the Act, the profits or gains of a business have to be ascertained by the ordinary commercial methods. If the argument advanced on behalf of the Crown be accepted, it would follow that no allowance could be claimed for instance for bad debts actually written off during the year, since there is no specific provision in Section 10 for allowing such deduction. But it could not be, and in fact was not, contended that allowance should not be made for such bad debts. The practice of making allowance for such bad debts has become firmly established. As the Court has to find out the amount of profits or gains of the business during the period, the question arises whether the loss by theft in question should be deducted when the profits are ascertained.

8. As pointed out in Konstam's book, The net profits of the trade or business should be computed by reasonable business methods, subject to any specific directions contained in the Income-tax Act.

9. Lord Herschell observed in Russell v. Town and County Bank (1888) 13 A.C. 418 at 424 as follows:

> The profit of a trade or business is the surplus by which the receipts from the trade or business exceed 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 'profits' can properly be applied.

10. Similar observations were made by Lord Parker in Usher's Wiltshire Brewery, Ltd. v. Bruce (1915) A.C. 433 at 458:

> 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.

11. It was argued for the assessee that the allowance claimed would come under Section 10(2)(ix) :

> Any expenditure (not being in the nature of capital expenditure) incurred solely for the purpose of earning such profits or gains.

12. It was also argued that in the case of money-lending business of Nattukottai Chetties, the loss in question must be taken to be loss of stock-in-trade. On the other side, it was argued for the Crown that the loss in question could not be said to be an expenditure incurred, much less, solely, for the purpose of earning such profits or gains, and that in any event it should be taken to be expenditure in the nature of "capital" expenditure. It was also argued that the monies in question could not be said to be "stock-in-trade" in the ordinary sense of the expression. Having regard to the way in which such people carry on their money-lending business, it would seem to be essential for the

successful carrying on of their business to have cash with them even after "the usual banking hours". They carry on their business operations, as is well known, even after the offices of the European Banks are closed for business for the day. Keeping monies with them for purposes of their trade after such office hours could not, therefore, in my view, be said to be anything else than keeping monies in the usual course of their business. The profits made by them by doing business after the usual office banking hours are surely liable to income-tax. The finding, as I understand it, is that in the usual course of business the remaining cash, etc., on hand and the jewels received on pledge from the customers were kept in the "strong room" of the business premises, and that thieves broke into the strong room and stole the cash and currency notes and the jewels. The fact of theft having been found, I think that the loss in question should be taken to be a loss connected with or arising out of the money-lending trade or business of the assessees. With reference to the jewels thus lost, the Income-tax authorities have, and, in my opinion, rightly, made allowance; but I think that allowance should be made also for the cash and currency notes amounting to Rs. 9,335 thus lost. I am unable to agree with the contention of the Crown that the loss in question, should, if at all, be taken to be loss of "capital". It is true, as pointed out on behalf of the assessees, that the profits of the Moulmeingyun business for the period in question was computed by the Income-tax authorities to be over Rs. 20,000. But that circumstance by itself is no ground for holding that the item in question should be taken as loss of profits, and not loss of capital. Whether a particular item is really capital expenditure or not has to be decided having regard to various considerations. Of course it is well established that when once profits have been earned during the period, it does not matter how the same is dealt with subsequently.

13. I am inclined to the view that in the case before us, the cash and currency notes, etc., lost, should be taken to be "stock-in-trade" of the assessee's business. What should be considered as stock-in-trade of a business should be decided after having regard to the nature of the particular business, its requirements, and other circumstances essentially connected with the successful carrying out of the particular business.

14. In Punjab National Bank v. Commissioner of Income-tax (1926) I.L.R. 7 L. 227: 2 I.T.C. 184 the question was raised whether allowance should be made for depreciation in the case of certain Government securities held by a firm. The answer would depend on the question whether those securities were held by the firm (Bank) with the object of dealing with them from day to day in the ordinary course of its business including that of buying and sellings Government securities in the usual course, or whether such Government securities were purchased by the firm (Bank) with the object of constituting the same as a sort of reserve in lieu of cash. In the case of the former, allowance should be made for depreciation (the reason being that the Government securities, should, in such a case, be treated as "stock-in-trade" of the Bank) ; but not in the case of the latter.

15. In the case of money-lending business such as the one before us, I think that the reasonable view to take as regards stock-in-trade is the one indicated by me before.

16. The decision in Jagarnath Therani v. Commissioner of Income-tax, Bihar and Orissa (1925) 2 I.T.C. 4, so far as it goes, also supports this view. There, some money was entrusted to a gumastha of a firm in the usual course of business with instructions to pay the same to a creditor of the firm. The

gumastha embezzled the monies. He : was criminally prosecuted, but was acquitted, his defence being that he was robbed of the money. The case in Jagamath Therani v. Commissioner of Income-tax, Bihar and Orissa (1925) 2 I.T.C. 4, however, was comparatively a plainer case than the one before us, and the Court, if one may say so with respect, very properly held that the loss was connected with and arose out of the business, and was not prima facie a loss in the nature of capital expenditure.

17. On behalf of the assessees, the decision of Rowlatt, J., in Curtis v. J. & Y. Oldfield, Ltd. 9 T.C. 319, was referred to before us. At page 330 the learned Judge observed as follows :

> I quite think, with Mr. Latter, that if you have a business, in the course of which you have to employ subordinates, and owing to the negligence or the dishonesty of the subordinates, some of the receipts of the business do not find their way into the till, or some of the bills are not collected at all, or something of that sort, that may be an expense connected with and arising out of the trade in the most complete sense of the word.

18. Stress was laid on the words "something of that sort" occurring in that judgment. But the words are too wide and one cannot be certain that the learned Judge had a case like the present in his view. Too much importance should not, I think, be attached to the above observation in the circumstances. It was argued on behalf of the Crown that theft should not be taken to be anything connected with or arising out of the assessee's money-lending business. In my view that is stating the position rather too broadly. In the case of Railway Administrations and other common carriers, the practice seems to be to make allowance for losses sustained by them in compensating passengers for accidents in travelling over the railway, etc. That the practice is to make such allowance in favour of common carriers is taken for granted in the judgment of Lord Loreburn, L.C., in Strong and Company, Lid. v. Woodifield (1906) A.C. 448 : 5 T.C. 215 At page 452 the Lord Chancellor observed as follows:

> In my opinion, however, it does not follow that if a loss is in any sense connected with the trade, it must always be allowed as a deduction; for it may be only remotely connected with the trade, or it may be connected with something else quite as much as or even more than with the trade. I think only such losses can be deducted as are connected with in the sense that they are really incidental to the trade itself. They cannot be deducted if they arc mainly incidental to some other vocation or fall on the trader in some character other than. that of trader. The nature of the trade is to be considered. To give an illustration,losses sustained by a railway company in compensating passengers for accidents in travelling might be deducted.

19. If losses sustained by a railway company in compensating passengers for accidents in travelling over its line could be deducted, it would seem to follow that losses similarly sustained by a railway company in compensating owners and consignees of goods entrusted to them for carriage, but which were lost during transit by theft, could also be deducted in proper cases. That could seem to resemble the present case, and the observations by the Lord Chancellor, I think prima facie, support

the contention of the assessee before us.

20. No doubt the further observations made by the Lord Chancellor should, also be kept in view. It was remarked later on at page 452:

> Many cases might be put near the line, and no degree of ingenuity can frame a formula so precise and comprehensive as to solve at sight all the cases that may arise.

21. The loss must be something in the nature of a commercial loss. Whether a particular loss is of that nature or not would have to be decided with reference to all the circumstances of a case. In Royal Insurance Co. v. Watson (1896-7) A.C. 1 Lord Shand expressed the opinion that damages awarded to an employee for wrongful dismissal would be allowable as a deduction. Damages for libel against a newspaper proprietor would appear to be loss in the ordinary course of business of proprietors of newspapers. See Pratt and Redman's Income-tax Law, 10th Edition, page 112.

22. To the argument urged on behalf of the Crown that it is no part of the assessee's business to deal with thefts, the following observations of Lord Buckmaster in Gliksten & Son, Ltd. v. Green (1929) A.C. 381 : 14 T.C. 365 may be referred to. There, the question was whether the amount received by a firm of timber merchants from fire insurance companies in respect of stock of timber destroyed by fire could be assessed to income-tax. At page 384 Lord Buckmaster observed as follows:

> If this results in a gain, as it has done, it appears to me to be an ordinary gain-a gain which has taken place in the course of their trade- none the less because, as Mr. Macmillan put it, and as I think Sir John Simen before him appears to have put it, it is no part of a timber merchant's business to trade in fires.

23. If, in the present case the stock-in-trade of the assessees before us including balance on hand each day and the jewels, etc., received on pledge from customers, had been insured at a particular figure against fire or theft, and the amount was accordingly received from the insurers on the occurrence of fire or theft, then the amount so received would, according to the decision in Gliksten & Son, Ltd. v. Green (1929) A.C. 381 : 14 T.C, 365 be prima facie taxable. The premia paid in respect of such insurance is allowed to the assessee [see Section 10(2)(iv)], and in return, the amount received by the assessee from the insurers would seem liable to be assessed to income-tax. If no insurance had been effected by the assessees, no premium is paid and no allowance is made on account of premium; and in case of loss, the assessee receives no amount from insurers, and therefore no such amount could be included in the assessment. The reasoning would seem to lead to the conclusion that the loss even if uninsured should be deducted, as I have come to the conclusion that the loss is connected with the business and is really incidental to the trade itself, having regard to the nature of the trade or business of the assessee.

24. Turning to the English Text-Books on Income-tax Law, I find the following statements in Sanders' Income-tax, 3rd, edition. At page 310 it is stated that "a deduction is allowed in respect of employees' theft." At page 196, it is stated, that "loss from embezzlement is deductible." Similarly at page 163, "deduction is allowed in practice for the loss arising from defalcations of employees." At

page 203, there are two passages which are rather important: "a deduction is permitted in practice for fire insurance premiums"; also, "loss of stock through fire is deductible in so far as it is not recovered by insurance, but loss of building does not form an admissible deduction." I also note that, "loss by flood or tempest" is allowed in case of assessments under Sch. A. The above statements, so far as they go, would seem to lend support to the assessees' contention in the present case.

25. Each case has to be decided with reference to the facts and circumstances relating thereto, and having regard to the nature and methods of trade or business in question. Having regard to the circumstances of the present case, and the findings of fact arrived at by the Income tax Commissioner, I think that the assessees are entitled to the deduction of Rs. 9,335 claimed by them, and I would answer the question in the affirmative.

Curgenven, J.

The question which the Commissioner refers is:

> Whether the loss incurred by theft of money used in the monev-lending business and in the business premises should be allowed for in computing the income-tax.

26. The Commissioner rightly observes that a loss of this character is not included within any of the deductions permissible under Section 10(2) of the Act. But that does not conclude the matter, because Section 10 provides for the taxation of the profits of a business, and we have therefore to consider whether, in computing profits, the amount of such a loss may be deducted from them. It is settled, for instance, that a bad debt incurred by a money-lender may be so deducted, on the ground that it is a loss incidental to his business, so that it is fair, in assessing his net profits, to take account of losses as well as gains. Such a loss, it appears to me, must satisfy two conditions: (1) it must be a loss of part of the stock-in-trade of the business, and (2) it must be a loss of such a kind as is incidental to the business.

27. As regards (1), the question describes the money lost as "money used in the money-lending business," and taking this to mean money actually in use in the carrying on of the business, I feel no difficulty in holding that it was part of the moneylender's stock-in-trade. It may have included profits earned in previous transactions, but if those profits were themselves to be applied to the business, and were kept in hand for that purpose, they would not, I think, be any the less part of the stock-in-trade.

28. Requirement No. (2) presents greater difficulties, because I think it is clear that not all kinds of losses of stock-in-trade can be said to be incidental to the business. A loss, to be incidental, must be such as in the ordinary course, and having due regard to the peculiar risks attendant upon the conduct of the business, is likely from time to time to occur. Cases of embez-zlement by subordinates, such as formed the subject of Jagar-nath Therani v. Commissioner of Income-tax, Bihar and Orissd (1925) 2 I.T.C. 4 would be losses of this nature, because the employment of clerks and servants is unavoidable, and the employer is likely, sooner or later, to be the victim of their

dishonesty or negligence. That such a loss might be classed as a form of expense arising out of trade was recognised in Curtis v. J. & Y. Old field, Ltd. 9 T.C. 319 although in the particular circumstances of that case, as I read it, the money lost no longer formed part of the stock-in-trade. The test whether the loss was, in the language of the English rule, "connected with or arising out of trade," was applied in two other English cases, Strong & Co., Ltd. v. Woodifield (1906) A.C. 448 : 5 T.C. 215 and Inland Revenue Commissioners v. Warnes & Co. (1919) 2 K.B. 444 : 12 T.C. 227 The former related to damages claimed from an inn-keeper in respect of injuries caused to a customer by the falling of a chimney; the latter to a penalty incurred by a trading firm for negligently failing to observe certain conditions imposed during Wartime on the export of goods to neutral countries. The loss was held, in the language of the English rule, to be a loss "not connected with or arising out of trade." These cases do not help us further than to show what manner of test should be applied. Now in the present case it may be conceded that a money-lender's business requires that he should keep a considerable sum in cash on his premises. Even if a bank is accessible to him, it would unduly restrict his activities to transact his affairs only within banking hours. The practice is certainly otherwise, and it is only fair to have regard to custom in deciding what the exigencies of a business require. That means that cash must be kept in a safe or strong room. The receptacle in the present case is described as a strong room and the question resolves itself into whether theft from a strong room may form the foundation of a claim to remission of tax. I exclude cases of theft by a clerk or servant employed in the business and having access to the strong room, because that is not in question here and special considerations might apply. In general, I am not prepared to say that theft by some external operator, with or without the complicity of domestic servants, ought to be recognised as the basis of a claim. To recognise it we must, I think, find not only that the cash had to be kept on the premises, but that its loss by theft was a circumstance which was so far probable as to be an occurrence incidental to, if not inseparable from, the manner in which it had to be kept. In my experience, the abstraction of money by theft from properly constructed safes or strong rooms is not within the competence of the ordinary thief or house-breaker, and we have not yet in this country to reckon with gangs of safe-breakers, such as may be found elsewhere. Perhaps the circumstance that no decision upon a case of this nature is to be found suggests the infrequency of such claims. ' The only test to apply, in order to see whether a loss of this kind is one incidental to the business, is, I think, the comparative likelihood of its occurrence, the requirements of the business being what they are. For example, injury to life and limb, and probably theft too, must occur sooner or later in the running of a railway. Bad debts and embezzlement have already been adverted to. Very likely the theft of stock-in-trade which have to be kept exposed to the public would fall into the same category. But I doubt whether cash kept in a safe should, if it should happen to be stolen, be allowed for.

29. We have not been furnished with any adequate narration of the facts of the present case, so that the question has had to be answered, as indeed it is put, in general terms. So considering it, I agree with my Lord in returning a reply in the negative.