1959

February 23.

THE COMMISSIONER OF INCOME-TAX, MYSORE, TRAVANCORE-COCHIN AND COORG, BANGALORE

v.

THE INDO MERCANTILE BANK, LIMITED

(and connected appeal)

(N. H. BHAGWATI, B. P. SINHA and J. L. KAPUR, JJ.)

Income Tax—Business Loss—Set off—Profits made in Travancore State—Losses incurred outside the State—Scope of the proviso to the main enactment—Travancore Income-tax Act, 1121 (Travancore XXIII of 1121), ss. 4, 9, 13, 18, 32(1), first proviso—Indian Income-tax Act, 1922 (XI of 1922), ss. 3, 4, 6, 10, 14, 24(1), first proviso.

Section 32(1) of the Travancore Income-tax Act, which corresponds to s. 24(1) of the Indian Income-tax Act, 1922, provided: "Where any assessee sustains a loss of profits or gains in any year under any of the heads mentioned in Section 9 [s. 6 of the Indian Act] he shall be entitled to have the amount of loss set off against this income, profits or gains under any other head in that year:

Provided that where the loss sustained is a loss of profits or gains which would but for the loss have accrued or arisen within British India or in an Indian State and would under the provisions of clause (c) of sub-section (2) of Section 18 [corresponding to s. 14 of the Indian Act] have been exempted from tax, such loss shall not be set off except against profits or gains accruing or arising within British India or in an Indian State and exempt from tax under the said provisions".

The assessees were companies having their head offices in the erstwhile State of Cochin with branches in the erstwhile State of Travancore and in other places outside the latter State. They made profits in Travancore State but incurred losses in Cochin State and other places, and for the purposes of assessment to income-tax they sought to deduct this loss from the profits made in Travancore State. The Income-tax Officer acting under the provisions of the Travancore Income-tax Act, determined the assessable income representing only the profits made in Travancore State and under s. 32(1), first proviso of the Travancore Income-tax Act [which corresponds to the first proviso to s. 24(1) of the Indian Income-tax Act, 1922] refused to allow a deduction of the losses incurred. The assessees claimed that the business

which they were carrying on was one and indivisible for the purpose of determining the amount assessable to income-tax and that they were entitled to a deduction of the losses incurred outside Travancore State. The contention on behalf of the income-tax authorities was (1) that under the first proviso to s. 32(1) of the Travancore Income-tax Act losses incurred in places outside the State of Travancore cannot be set off against profits made in that State, (2) that though profits and losses in the State arising under the same head could be set off, the proviso, aforesaid, affected not only the generality of the main enactment but also introduced an addendum that where the profits of the business arose in the State and the losses under the head business were sustained outside that State, those losses could not by virtue of the proviso be deducted from profits made in the State, (3) that the proviso applied only to the head "business" in the two respective territories, as the words used therein are "where the loss sustained is a loss of profits or gains" and the word "income" is not mentioned therein, and (4) that the word "business" in s. 13 of the Travancore Act corresponding to s. 10 of the Indian Act, must mean business in Travancore State under s. 13 of that Act and "business in British India" under the Indian Act, because before 1939 income was not chargeable under the two Acts, unless it was received or accrued in Travancore State or British India, as the case may be, and profits and gains of business in territories outside Travancore or in an Indian State were exempted from payment of income-tax in Travancore State or in British India, as the case may be.

Held: (1) Under s. 24(1) of the Indian Income-tax Act, 1922 [s. 32(1) of the Travancore Income-tax Act] a set off can be claimed only when the loss arises under one head and the income, profits and gains against which it is sought to be set off arises under a different head. In cases where profits and losses arise under the same head they have to be adjusted against each other under the provisions of ss. 7 to 12B of the Indian Act.

Arunachalam Chettiar v. *Commissioner of Income-tax*, (1936) L.R. 63 I. A. 233 and *Anglo-French Textiles Co., Ltd.* v. *Commissioner of Income-tax, Madras*, [1953] S.C.R. 448, relied on.

(2) The territory of a proviso is to carve out an exception to the main enactment and exclude something which otherwise would have been within the section; it has to operate in the same field and if the language of the main enactment is clear it cannot be used for the purpose of interpreting the main enactment or to exclude by implication what the enactment clearly says unless the words of the proviso are such that that is its necessary effect.

Abdul Jabar Butt v. *State of Jammu and Kashmir*, [1957] S.C.R. 51, *Ram Narain Sons Ltd.* v. *Assistant Commissioner of Sales Tax*, [1955] 2 S.C.R. 483, *Madras & Southern Mahratta Railway Co.* v. *Bezwada Municipality*, (1944) L.R. 71 I.A. 113

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and *Corporation of the City of Toronto* v. *Attorney-General for Canada*, [1946] A.C. 32, relied on.

Consequently, s. 24(1), first proviso, of the Indian Income-tax Act, 1922 [s. 32(1), first proviso, of the Travancore Act] bars the right of set off only where a loss in the Indian States under one head is sought to be set off against profits in British India under any other head, and does not apply to profits and losses and computation thereof which fall under s. 10 of the Indian Act, corresponding to s. 13 of the Travancore Act.

(3) The mere fact that the word "income" is not used in the proviso does not justify the construction that the intention of the Legislature was to restrict the right to a set off of profits and losses arising in Indian States only to business or to modify the mode of computation under s. 10 of the Indian Income-tax Act.

(4) The word "business" in s. 10 of the Indian Income-tax Act, 1922, is not confined to business in British India, in view of the definition of "total income" and "total world income" and chargeability of total income under s. 3, or the provisions of s. 4 where in the case of a resident "total income" includes income, profits and gains accruing within or without British India.

CIVIL APPELLATE JURISDICTION: Civil Appeals Nos. 259 and 260 of 1958.

Appeals by special leave from the judgment and orders dated August 5, 1955, of the former Travancore-Cochin High Court in Income-tax Reference Appeals Nos. 6 of 1953 and 21 of 1954.

K. N. Rajagopala Sastri, *R. H. Dhebar* and *D. Gupta*, for the appellant.

G. B. Pai and *Sardar Bahadur*, for the respondent in C. A. No. 259 of 1959.

A. V. Viswanatha Sastri and *Naunit Lal*, for the respondents in C. A. No. 260 of 1958.

1959. February 23. The Judgment of the Court was delivered by

Kapur J.

KAPUR, J.—These two appeals by special leave raise a common question of law, and that is, whether business losses incurred in the erstwhile State of Cochin could, under the Income-tax Act of Travancore, be set off against the business profits made in the erstwhile State of Travancore. In Appeal No. 260/58 a further question arose whether in the case of

that assessee the year ending June 30, 1949, was the previous year for the assessment year 1950-51 with the result that it should be assessed under the Indian Income-tax Act of 1922. But this question was not answered by the High Court which confined itself to answering the first question which was common to both the appeals. The appellant before us in both the appeals is the Commissioner of Income-tax and the respondents are the two assessees, in one case a Bank and the other a private limited company. The main argument has been confined to the question of applicability of s. 32(1) and the first proviso to that section of the Travancore Income-tax Act (hereinafter called the Travancore Act).

In C. A. No. 259/58 the assessee is a public limited company incorporated in the State of Cochin with branches in that State as well as in what was British India and in Travancore State. It filed its income-tax return showing an income of Rs. 11,872 for the assessment year 1948-49, its accounting year being the previous calendar year. The Income-tax Officer determined its assessable income to be Rs. 90,947 representing only the profit it made in Travancore State and under s. 32(1) proviso (i) of the Travancore Act he refused a deduction of Rs. 79,275 shown as loss from branches situate outside the State of Travancore, in British India and other Indian States. The assessee's appeal to the Income-tax Commissioner was unsuccessful but the Appellate Tribunal held that the banking business of the assessee being one and indivisible for the purpose of determining the amount assessable to income-tax it was entitled to deduct the losses incurred outside Travancore State from the profits accruing and arising in that State. At the instance of the Commissioner of Income-tax the following question was referred to the High Court of Travancore-Cochin :—

" Is the aforesaid sum of Rs. 79,275 a loss of the assessee arising outside the Travancore State for purpose of the first proviso to section 32(1) of the Travancore Income-tax Act ? "

This question was slightly modified by the High Court

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which after referring to several decided cases answered the question in favour of the assessee.

In C. A. 260/58 the assessee is a private limited company with its registered office in the former Cochin State. It was carrying on business at its head office in Cochin State and it also carried on business in Travancore State. The assessment was made under the Travancore Act and relates to the previous year ending June 30, 1949, the assessment year being 1950-51. The assessee made a profit in Travancore State and incurred a loss in the State of Cochin and sought to deduct this loss from the profit of Travancore State thus showing a net profit of Rs. 2,643. This was not allowed by the Income-tax Officer and on appeal this order was confirmed by the Appellate Assistant Commissioner. The Appellate Tribunal also did not accept the submissions of the assessee and upheld the order of assessment. On an application of the assessee the following question was referred to the High Court of Travancore-Cochin :—

" Whether on the facts and in the circumstances of the case the loss of Rs. 27,709 arising in Cochin State could be set off against the profit of Rs. 38,998 arising in Travancore State ? "

and was answered in favour of the assessee. The Commissioner has come up in appeal pursuant to special leave against both these judgments.

It may be stated that the relevant sections of the Travancore Act which govern the two appeals are identically worded with those of the Indian Income-tax Act of 1922 (to be called the Indian Act). The corresponding sections are as follows :

Headings	Sections in Travancore Act.	Section in Indian Act.
Application of the Act	4	4
Head of income chargeable to income-tax	9	6
Business	13	10
Exemptions of a general nature	18	14
Set off of loss in computing aggregate income	32	24

It is only necessary to set out s. 32(1) of the Travancore Act and the proviso which correspond to s. 24(1) and proviso (i) of the Indian Act and which are necessary for the decision of the appeals before us:

S. 32(1) "Where any assessee sustains a loss of profits or gains in any year under any of the heads mentioned in Section 9 (Section 6) he shall be entitled to have the amount of loss set off against this income, profits or gains under any other head in that year:

Provided that where the loss sustained is a loss of profits or gains which would but for the loss have accrued or arisen within British India or in an Indian State and would under the provisions of clause (c) of sub-section (2) of Section 18 (Section 14(2)(c)), have been exempted from tax, such loss shall not be set off except against profits or gains accruing or arising within British India or in an Indian State and exempt from tax under the said provisions". (Sections in brackets are the corresponding sections of the Indian Act).

So the only difference between the two sections is that in the proviso to s. 24(1) of the Indian Act instead of the words "an Indian State" the words "British India or in an Indian State" have to be substituted. The question for decision is as to how this proviso is to be construed. Ordinarily the effect of an excepting or a qualifying proviso is to carve something out of the preceding enactment or to qualify something enacted therein which but for the proviso would be in it and such a proviso cannot be construed as enlarging the scope of an enactment when it can be fairly and properly construed without attributing to it that effect. *Corporation of the City of Toronto* v. *Attorney-General for Canada* (1). But it has been held that a section framed as a proviso to a preceding section may sometimes contain matter which is in substance a fresh enactment adding and not merely qualifying that which goes before. *Rhondda Urban Council* v. *Taff Vale Railway* (2).

It was argued on behalf of the Revenue that this

(1) [1946] A.C. 32, 37. (2) [1909] A.C. 253, 258.

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proviso falls in the second category and takes the present cases out of s. 32(1) of the Travancore Act and imposes a liability to tax on the profits or gains arising in that State, disallowing a deduction of the losses in British India and in States other than Travancore State against profits made in Travancore State: *Rhondda Urban Council* v. *Taff Vale Railway* (1) and *Harrison* v. *Ward* (2). It may be mentioned that in the majority of cases decided in India the proviso to s. 24(1) of the Indian Act has been construed in a manner contrary to the submissions made on behalf of the Revenue.

In order to determine the true meaning of the words of the proviso it is necessary and convenient to refer to the scheme of the Indian Act which is admitted by the parties to be same as that of the Travancore Act. From 1922 to 1939 in order to be taxable income, profits and gains had to be received or had to accrue in British India. In 1939 the idea of 'total world income' was introduced and the definition of 'total income' was modified by the Indian Income-tax (Amendment) Act (VII of 1939) which also made consequential changes in other sections of the Indian Act. Under s. 2(15) of the Act 'total income' was defined to mean the total amount of income, profits and gains computed in the manner laid down in that Act. The 'total world income' was defined as including all income, profits and gains wherever accruing or arising except income to which the Act did not apply. Section 3 provided for the charge of income-tax in respect of the total income of the previous year. Under s. 4 the total income of any previous year of any person who was resident included all income, profits and gains from whatever source derived but (i) it must accrue or arise to him during the year in British India or (ii) accrue or arise to him without British India during such year. The third clause is not necessary for this appeal. Section 4(3) provided what income, profits or gains were not to be included in the total income of the person receiving them. Both under the Indian Act and under the Travancore Act

(1) [1909] A.C. 253, 258. (2) [1922] 1 Ch. 517.

there were six heads of income chargeable to income-tax. In the Indian Act they were set out in s. 6 as follows:—

S. 6 "Save as otherwise provided by this Act the following heads of income, profits and gains shall be chargeable to income-tax in the manner hereinafter appearing, namely:—

.....

.....

.....

(iv) Profits and gains of business, profession or vocation.

.....

....."

Then followed ss. 7 to 12B laying down the method of computation of the income arising from each head.

In 1941 during the war an exemption was given for the purpose of taxability to any income, profits or gains which accrued or arose within what was then called Indian States but which were not received or brought into British India. This was done by s. 8 of the Indian Income-tax (Amendment) Act, 1941 (XXIII of 1941) by which another clause (c) was added to s. 14(2) which was as follows:

"The tax shall not be payable by an assessee:

.....

.....

(c) in respect of any income, profits or gains accruing or arising to him within (an Indian State) unless such income, profits or gains are received or deemed to be received in or are brought into the Indian State in the previous year by or on behalf of the assessee or are assessable under section 12B or section 42".

Thus income, profits or gains arising under any of the heads under s. 6 became exempted in circumstances above-mentioned but the effect of this exemption was not to exclude such income of an assessee for all purposes as was the case under s. 4(3). Such sums were to be taken into account for the purpose of determining the rate under s. 16 of the Indian Act. A further consequential change was made in s. 24(1) by

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the addition of the first proviso and a similar addition was made in the Travancore Act to s. 32(1) which has already been quoted and it is this proviso which is the subject-matter of controversy between the parties. A review of the various sections and enactments shows that during 1922-1939 the tax was leviable on income, profits and gains arising or accruing to an assessee in British India. In 1939 the total income became taxable subject to exclusions in sub-s. 3 of s. 4 and the chargeability of the 'total income' was laid down in s. 3. In 1941 income, profits or gains which a resident made in an Indian State and in the case of Travancore State income, profits or gains which a resident made in British India or other Indian States were exempted from payment of income-tax unless received or brought into the respective territories, but this income, profits or gains had to be included for the purpose of calculating the rate.

Now we come to s. 24(1). This section was introduced in 1922 before which under the Indian Act of 1918 a loss under one head of income could not be set off against income under another head, the taxability of income arising from each head being separate. By the addition of this section the loss under one head of profits or gains was allowed to be set off against income, profits and gains under any other head in any assessment year. There was also a provision in s. 24(2) for carrying over the loss after such set off had been effected. Section 24(1) became the subject matter of controversy in the courts. The Privy Council in *Arunachalam Chettiar* v. *Commissioner of Income-tax* (1) held that this section was meant for a set off of profits arising under different heads and not where profits and losses had to be adjusted if they arose under the same head. Sir George Rankin said at p. 241:

"In their Lordships' opinion, whether a firm is registered or unregistered, partnership does not obstruct or defeat the right of a partner to an adjustment on account of his share of loss in the firm, whether the set off be against other profits under the same

(1) (1936) L.R. 63 I.A. 233.

head of income within the meaning of s. 6 of the Act or under a different head (in which case only need recourse be had to s. 24, sub-s. 1)".

Thus the Privy Council emphasised that the object of s. 24(1) was to allow a set off of profits against losses arising under different heads and only in such cases could recourse be had to s. 24(1). In cases where profits and losses arose under the same head they had to be adjusted against each other. This Court in *Anglo-French Textiles Co. Ltd.* v. *Commissioner of Income-tax, Madras* (1) again emphasised that distinction in the following words:—

"Next, a set off under section 24(1) can only be claimed when the loss arises under one head and the profits against which it is sought to be set off arises under a different head. When the two arise under the same head, of course the loss can be deducted but that is done under section 10 and not under section 24(1)". (Per Bose, J.)

Indeed it is not disputed that when profit and loss arose under the same head in any place which was not an Indian State recourse had to be had to the provisions of ss. 7 to 12B and not to any other section. But it was contended on behalf of the Revenue that the first proviso to s. 24(1) of the Indian Act not only affected the generality of the main enactment but also introduced an addendum that where the profits of the business arose in what was British India in the case of the Indian Act or what was Travancore State in the case of the Travancore Act and the losses under the head business were sustained in an Indian State or in the latter case in any other Indian State or British India, these losses could not by virtue of the proviso be deducted from profits made in British India or Travancore State as the case may be. They could only be adjusted against profits arising in an Indian State or in the case of Travancore State in British India or another Indian State. Thus the proviso, it was contended, was a modification of the method of computation under s. 10(2) of the Indian Act for

(1) [1953] S.C.R. 448, 453.

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determining profits and gains of the business of any resident. We should be averse to lend any countenance to such a mode of construing a proviso unless the language used expressly or by necessary intendment leads to that conclusion. The proper function of a proviso is that it qualifies the generality of the main enactment, by providing an exception and taking out as it were, from the main enactment, a portion which, but for the proviso would fall within the main enactment. Ordinarily it is foreign to the proper function of a proviso to read it as providing something by way of an addendum or dealing with a subject which is foreign to the main enactment. "It is a fundamental rule of construction that a proviso must be considered with relation to the principal matter to which it stands as proviso". Therefore it is to be construed harmoniously with the main enactment. (Per Das, C. J.) in *Abdul Jabar Butt* v. *State of Jammu & Kashmir* (1). Bhagwati, J., in *Ram Narain Sons Ltd.* v. *Assistant Commissioner of Sales Tax* (2) said:

"It is a cardinal rule of interpretation that a proviso to a particular provision of a statute only embraces the field which is covered by the main provision. It carves out an exception to the main provision to which it has been enacted as a proviso and to no other".

Lord Macmillan in *Madras & Southern Mahratta Railway Co.* v. *Bezwada Municipality* (3) laid down the sphere of a proviso as follows:—

"The proper function of a proviso is to except and deal with a case which would otherwise fall within the general language of the main enactment, and its effect is confined to that case. Where, as in the present case, the language of the main enactment is clear and unambiguous, a proviso can have no repercussion on the interpretation of the main enactment, so as to exclude from it by implication what clearly falls within its express terms".

The territory of a proviso therefore is to carve out an

(1) [1957] S.C.R. 51, 59. (2) [1955] 2 S.C.R. 483, 493.
(3) (1944) L.R. 71 I.A. 113, 122.

exception to the main enactment and exclude something which otherwise would have been within the section. It has to operate in the same field and if the language of the main enactment is clear it cannot be used for the purpose of interpreting the main enactment or to exclude by implication what the enactment clearly says unless the words of the proviso are such that that is its necessary effect. (Vide also *Corporation of The City of Toronto* v. *Attorney-General for Canada*) (1).

In the proviso in dispute there are no positive words which would support an interpretation in favour of the disintegration of the head " business " and compel the application of the proviso to the same head, specially keeping in view the object of the main section, i.e., s. 24(1) which was to set off loss of profits or gains under one head against income, profits or gains under any other head.

It was then submitted that in the proviso the words used were " where the loss sustained is a loss of profits or gains " and therefore it necessarily applied to the head " business " in the two respective territories. But in the main enactment itself, i.e., s. 24(1) of the Indian Act the words used are " a loss of profits or gains ". The mere fact that the word " income " is not used does not justify the construction that the intention of the Legislature was to restrict the set off of profits and losses arising in Indian States only to business or to modify the mode of computation under s. 10 of the Indian Act. That the use of these words does not circumscribe the proviso to business alone is shown by the difference in the language of the proviso to sub-s. (2) of s. 24 of the Indian Act:—

S. 24 (2).....

" provided that

(a) where the loss sustained is a loss of profits and gains of a business 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

(1) [1946] A.C. 32, 37.

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off except against profits and gains accruing or arising in (an Indian State) from the same business, profession or vocation and exempt from tax under the said provisions".

That proviso shows that where the Legislature wanted to restrict the losses and profits or gains to business alone they specifically said so. It is significant that in ss. 2(13) and (5) of the Indian Act of 1918 corresponding to ss. 2(15) and 6 of the Indian Act of 1922 the word used was "income" which in the latter Act was expanded into "income, profits and gains". The Privy Council said in the *Commissioner of Income-tax*, v. *Shaw Wallace and Co.* (1) that "the object of the Indian Act is to tax "income" a term which it does not define. It is expanded no doubt into "income, profits and gains" but the expansion is more a matter of words than of substance". It was also so said in *Commissioner of Income-tax, Bengal* v. *Mercantile Bank of India Ltd.* (2). See also *London County Council* v. *Attorney-General* (3). Thus the mere use of the words loss of profits or gains to be set off against profits and gains would not be sufficient to restrict the scope of the proviso to the profits and losses arising under the head business in the two territories, i. e., British India and the Indian States.

On behalf of the Revenue an alternate argument was raised for which support was sought from two decisions of the Allahabad High Court in *In Re*: *Mishrimal Gulabchand* (4) and *Raghunath Parshad* v. *Commissioner of Income-tax* (5). There it was held that s. 10 of the Indian Act had to be read with s. 14(2) (c) and if profits could not be added for the purposes of 'total income' losses sustained also could not be deducted. Counsel for the Revenue did not go to this extent that because profits were exempted losses could not be deducted; his argument was that because before 1939 income was not chargeable unless it was received or accrued in British India therefore business in s. 10 could only mean business in British India. But this

(1) (1932) L.R. 59 I.A. 206, 212. (2) (1936) L.R. 63 I.A. 457.
(3) [1901] A.C. 26. (4) [1950] 18 I.T.R. 75.
(5) [1955] 28 I.T.R. 45.

argument does not take note of the definition of 'total income', 'total world income' and chargeability of total income under s. 3 or the provisions of s. 4 where in the case of a resident 'total income' includes income, profits and gains accruing within or without British India. Therefore to say that business in s. 10 means business in British India or business the profits or gains of which are taxable in British India is to ignore the definitions and ss. 3, 4 and 6. Section 10 of the Indian Act does not distinguish between business in British India and business in an Indian State or so divide business. But then it was said that as the profits or gains of business in an Indian State were exempted from payment of tax in British India business in s. 10 must mean business in British India. That would be straining the language of s. 10 and would necessitate addition of words in s. 10 which are not there in the section.

In the course of argument a number of cases of the various High Courts were cited and criticised. We find it unnecessary to refer to them because we have indicated above what is the correct sphere of a proviso and what proviso (i) to s. 24(1) means.

In our view the question referred to the High Court which is common to the two appeals was rightly answered in favour of the assessee. As to the second question in Civil Appeal No. 260 of 1958 we do not propose to say anything. It will be open to the assessee in that appeal to take such steps in regard to that question as it may be advised.

In the result the appeals fail and are dismissed with costs.

Appeals dismissed.