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entitled to the rebate claimed by it. The appeal therefore fails and is dismissed with costs.

Appeal dismissed.

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October, 25.

A. V. THOMAS & CO., LTD., ALLEPPEY

v.

THE COMMISSIONER OF INCOME-TAX, (BANGALORE) KERALA

(J. L. KAPUR, M. HIDAYATULLAH and J. C. SHAH, JJ.)

Income Tax—Deduction—Bad debt—Expenditure—Amount advanced for purchase of shares—Indian Income-tax Act, 1922 (11 of 1922), ss. 10(2) (xi) and (xv).

The assessee company was incorporated in 1935 and its Memorandum of Association authorised it, *inter alia*, to promote and to undertake the formation and establishment of other companies and to assist any company financially or otherwise. There was another company known as the Southern Agencies Ltd. and Mr. A. V. Thomas was director of both these companies. In 1948 the Southern Agencies Ltd. began the promotion of a company to be known as the Rodier Textile Mills Ltd., with a view to buying up a Mill known as the Rodier Textile Mills. The assessee company made an advance of Rs. 6 lakhs odd to the promoter for the purchase of 6000 shares of the new company. The public took no interest in the new company and the whole project failed. No application for shares was made on behalf of the assessee company and no share was acquired. The Southern Agencies Ltd., however, did not return the entire amount. On December 7, 1951, it paid back only Rs. 2 lakhs which was received in full satisfaction. The balance of Rs. 4,05,071-8-6 was written off on December 31, 1951, which was the close of the year of account of the assessee company. For the assessment year 1952-53 the assessee company claimed a deduction of that amount as a bad debt actually written off, or alternatively as an expenditure, not of a capital nature laid out or expended wholly and exclusively for the purpose of its business.

Held, (1) that the amount advanced for the purchase of shares was of a capital nature and, therefore, the balance was not allowable as an expenditure under s. 10(2)(xv) of the Indian Income-tax Act, 1922, as it was not the business of the assessee company to buy agencies and sell them; and in any event the amount was expended in 1948 and not in the year of account ending December 31, 1951.

(2) that it was not a bad debt under s. 10(2)(xi). A debt in such cases is an outstanding which is recovered would have swelled the profits. It is not money handed over to some one for purchasing a thing which that person has failed to return even though no purchase was made.

Curtis v. *J. & G. Oldfield Ltd.*, (1925) 9 Tax Cas. 319, *Arunachalam Chettiar* v. *Commissioner of Income-tax*, (1936) L. R. 63 I. A. 233, *Badridas Daga* v. *Commissioner of Income-tax*, [1959] S. C. R. 690 and *Commissioner of Income-tax* v. *Abdullabhai Abdulakadar*, [1961] 2 S.C.R. 949, relied on.

CIVIL APPELLATE JURISDICTION : Civil Appeal No. 214 of 1962.

Appeal from the judgment dated July 8, 1960 of the Kerala High Court, Ernakulam, in Income-tax Referred Case No. 10 of 1957.

S. T. Desai and *Sardar Bahadur*, for the appellant.

K. N. Rajagopal Sastry, R. N. Sachthey and *P. D. Menon*, for the respondent.

1962. October 25. The Judgment of the Court was delivered by

HIDAYATULLAH, J.—The assessee, A.V. Thomas & Co., Ltd., Alleppey, claimed a deduction of Rs. 4,05,072-8-6 in the assessment year 1952-53 as a bad debt which was written-off in its books of account on December 31, 1951. This claim was disallowed. After sundry procedure, the following question was considered by the High Court of Kerala and answered against the assessee company :— *Hidayatullah, J.*

"Whether on the facts and the circumstances of the case, the Tribunal was correct in holding

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that the amount of Rs. 4,05,071-8-6 claimed by the assessee Co. as a deduction was not admissible either under section 10(2) (xi) or 10(2) (xv) ?"

The High Court certified the case as fit for appeal to this Court and this appeal has been filed by the assessee company. The Commissioner of Income-tax (Bangalore) Kerala, is the respondent.

The assessee company was incorporated in 1935 and, as is usual with companies, its Memorandum of Association, authorised it to do multifarious businesses. According to clauses 1, 5, 18 and 23, it was authorised "to be interested in, to promote, and to undertake the formation and establishment of other companies", to make investments and to assist any company financially or otherwise. At the material time the assessee company had three directors, whose names are given below :

1. A. V. Thomas
2. S. Sankaranarayana Iyer and
3. J. Thomas.

There was another private limited company known as the Southern Agencies Limited, Pondicherry, and its directors were :—

1. A. V. Thomas
2. S. S. Natarajan, and
3. C. S. Ramakrishna Karayalar.

There was a mill in Pondicherry known as Rodier Textile Mill belonging to the Anglo French Textiles Limited, Pondicherry. The assessee company averred that the Southern Agencies Ltd., took up in 1948 the promotion of a limited company to be known as Rodier Textile Mills Ltd., Pondicherry, with

a view to buying and developing the Rodier Textile Mill. The assessee company, so it was stated, financed the Southern Agencies Ltd., Pondicherry, by making over funds aggregating to the sum of Rs. 6,05,071-8-6. This amount was not given directly by the assessee company but at its instance by India Coffee and Tea Distributors Ltd., Madras. The assessee company further stated that though an entry in its own books dated December 31, 1948, showed this amount as an advance for purchase of 6,000 shares of Rs. 100 each in the Rodier Textile Mills Ltd., the main intention of the assessee company was to assist and finance the Southern Agencies Ltd. within the terms of the assessee company's Memorandum. The subscription list for the Rodier Textile Mills Ltd. remained open from January 5 to January 20, 1949. No application for shares was made on behalf of the assessee company and the shares were not acquired. The public took no interest in the new company which was being promoted and the whole project failed.

On September 1, 1950, the assessee company approved of the action of Mr. A. V. Thomas in making the said advance and on September 18, 1950, a resolution was passed by the Board of Directors of the assessee company that the amount of Rs. 6,00,000 should be shown as an advance for purchase of shares in the Rodier Textile Mills Ltd. (in formation) and the balance of Rs. 5,072-8-5 be shown under sundry advances due from the promoters of the new company. The Southern Agencies Ltd. however, did not return the entire amount. On December 7, 1951, it paid back Rs. 2,00,000 which appears to have been received in full satisfaction. Though as late as June 12, 1951, the advance was considered to be good and recoverable, the balance was written off on December 31, 1951, which was the close of the year of account of the assessee company. It was this amount which was claimed in the assessment year 1952-53 as a bad

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debt actually written off, or alternatively as an expenditure, not of a capital nature, laid out or expended wholly and exclusively for the purpose of the assessee company's business.

The Income-tax Officer, Alleppey, held that the debt was written off at a time when it was neither bad nor doubtful and the claim to write it off was premature. He, therefore, disallowed it. An appeal was taken to the Appellate Assistant Commissioner and he upheld the order of the Income-tax Officer though on a different ground. He held that the advance was made for the purpose of purchasing shares of the new company then in formation and it was thus made for the acquisition of a capital asset, which was either the control of the new company or "to gain its good-will likely to result in the grant of agency rights" to the assessee company. According to the Commissioner, the loss, if any, was of a capital nature and the question whether the claim of bad debt was premature or otherwise did not arise for consideration. The Appellate Assistant Commissioner also held that the deduction could not be claimed as an allowance under s. 10(2)(xv) of the Income-tax Act. The assessee company appealed to the Tribunal. The Tribunal upheld the order of the Appellate Assistant Commissioner but on a third ground. The Tribunal accepted that one of the objects of the assessee company was the promotion and financing of other companies for gain but this advance of Rs. 6,00,000 was not made by the assessee company in the normal course of its business. It was rather a transaction "actuated only by personal motives". In reaching this conclusion the Tribunal observed that the advance was made to Southern Agencies Ltd. which was not a company promoted by the assessee company, that between these two companies there was no previous business connection and that the assessee company had no expectancy of a financial benefit. The Tribunal held that the

Rodier Textile Mills Ltd., Pondicherry, was not being financed or promoted by the assessee company and that the statement by the assessee company that it would have received some agency right was not supported by evidence. The Tribunal was of the opinion that this advance was probably due to the "substantially common ownership of the assessee company and the Southern Agencies Ltd., of two individuals, namely, A. V. Thomas and S. S. Natarajan." The Tribunal thus held that this deduction could not be claimed as it was given out of "personal motives" and not as a part of the business of the assessee company.

The assessee company demanded a case but it was refused by the Tribunal. The assessee company in its application for the case had propounded three questions as under :—

"(i) Whether on the facts and in the circumstances of the case, the sum of Rs. 4,05,072-8-5 can be claimed by the assessee as a bad debt written off under the provisions of Section 10(2) (xi) of the Act,

(ii) Whether on the facts and in the circumstances of the case, the assessee can claim the sum of Rs. 4,05,072-8-5 as permissible deduction under Section 10(2) (xv) of the Act, and

(iii) Whether on the facts and in the circumstances of the case, the assessee is permitted to claim the deduction of the said sum of Rs. 4,05,072-8-5 as a proper debit and charge it to the Profit and Loss account of the assessee company."

These questions show that the deduction was claimed (i) as a loss in the doing of the business under

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s. 10(1); (ii) as a bad debt actually written off under s. 10(2)(xi); and (iii) as an expenditure laid out wholly and exclusively for the purpose of the business under s. 10(2)(xv) of the Income-tax Act. The assessee company applied to the High Court and the High Court directed a reference on the single question which has been quoted. That question shows that the High Court did not direct the case under s. 10(1) of the Act. The Tribunal had considered the case from the point of view of the business and had held that this was not an advance in the normal course of business but one out of "personal motives". The High Court apparently had not accepted that the matter could be considered under s. 10(1) and framed the question under cls. (xi) and (xv) of s. 10(2). The question as propounded and considered by the High Court related to the two clauses only. An attempt was made before us to raise the issue under s. 10(1) and to claim the deduction as an ordinary business loss. We disallowed the argument because in our opinion the question as considered in the High Court does not embrace it. The assessee company should have requested the High Court at some stage to frame a question that there was no material for the Tribunal to reach the conclusion that this was not a business transaction but a case of an advance out of personal motives. It was contended before us that the High Court in calling for a reference on the single question had stated that that question would cover three matters. The first two were mentioned in the question and the third which was said to be implicit was whether the Tribunal was competent to decide a case which had not been made out by the Department at an earlier stage. But this was not the same thing as saying that the Tribunal had no material before it on which it could reach the conclusion that this was not an advance in the ordinary course of business by the assessee company. No doubt, the High Court in its order calling for a statement of the case has observed that there was no dispute at any

earlier stage that this was not in the ordinary course of business, but that conclusion of the High Court in the order it made under s. 66(2) can have no relevance or binding force. Indeed, the High Court was in error in giving a finding of its own and it is not surprising that the Tribunal protested against this finding. It was open to the High Court to frame a question whether there was any material to support the finding of the Tribunal and to ask the Tribunal to state a case thereon. Not having done so, the question as framed drives the assessee company to prove its case either under s. 10(2)(xi) or under s. 10(2)(xv) and it is from these two angles that the case will be considered by us. Clauses (xi) and (xv) of s. 10(2) read as follows :—

"(2) Such profits or gains shall be computed after making the following allowances, namely :—

x x x x

(xi) when the assessee's accounts in respect of any part of his business, profession or vocation are not kept on the cash basis, such sum, in respect of bad and doubtful debts, due to the assessee in respect of that part of his business, profession or vocation, and in the case of an assessee carrying on a banking or money-lending business, such sum in respect of loans made in the ordinary course of such business as the Income-tax Officer may estimate to be irrecoverable but not exceeding the amount actually written off as irrecoverable in the books of the assessee :

(Proviso omitted)

(xv) any expenditure (not being an allowance of the nature described in any of the clauses (i) to (xiv) inclusive, and not being in the nature of capital expenditure or

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personal expenses) laid out or expended wholly and exclusively for the purpose of such business, profession or vocations".

In support of its case, the assessee company stated that as there was no dispute about the facts that this was an advance in the ordinary course of business it should be treated as a trading loss or alternatively as a bad debt or an expenditure claimable under s. 10(2)(xv). The assesses company relied strongly upon certain Ledger entries of the Rodier Textile Mills Ltd. in the books of the assessee company. These have been marked as Annexures A. 1 to A. 3. The High Court also referred to these accounts and they have been construed as showing that there was an attempt by the assessee company to acquire a capital asset. These accounts began in 1948 and ended on December 31, 1951. The accounts are headed "Personal Ledger." In December, 1948, sundry amounts totalling Rs. 6,05,071-8-5 are shown as amounts "paid *to you* by Indian Coffee and Tea Distributors Ltd., Madras, towards purchase of shares." On January 1, 1949, the account opened with a debit balance of Rs. 6,05,071-8-5. Nothing appears from the accounts who this "you" was. A number of reversing entries were made in respect of certain amounts and then on December 31, 1949, the amount was shown as follows :—

By advance for sundry expenses due from the promoters of new company debited to this transferred	5,071-8-5
By balance	6,00,000-0-0
1950 opened with entry on January 1—	
To Balance	6,00,000-0-0
and closed with an entry	
By Amount paid to Southern Agencies Ltd.	6,00,000-0-0

This was shown as an opening balance on January 1, 1951. On December 7, a payment of Rs. 2,00,000 was shown and Rs. 4,00,000 were transferred for writing off. On December 31, 1951, Rs. 4,00,000 were written off and so also the amount of Rs. 5,072-8-5. The last amount included a sum of Rupee 1, hire for carriage which was also written off after the entry had been reversed.

From these accounts it is quite clear that to begin with the amount was shown as an advance for purchase of shares of the Rodier Textile Mills Ltd. If this was the purpose, it was not an expenditure on the revenue side. The High Court correctly pointed out that it was not the business of the assessee company to buy agencies and sell them. The shares were being acquired by the assessee company so that it might have the lucrative business of selling agency and similar other agencies from the Rodier Textile Mills Limited. As late as December 15, 1952, the Chairman of the assessee company stated in his speech as follows :—

> "You are aware that an advance was made to the Southern Agencies (Pondicherry) Ltd. to acquire for us shares in Rodier Textile Mills Ltd. It was felt that when the promotion and working of Rodier Textile Mills Ltd., became a fait accompli, our company stood considerably to gain by securing their agency for handling their goods."

This clearly shows that the assessee company intended to acquire a capital asset for itself. This purpose takes the case of the assessee company out of s. 10(2)(xv) of the Income-tax Act, because no expenditure can be claimed under that clause which is of a capital nature. By the declaration of the Chairman of the assessee company the case under s. 10(2)(xv) becomes completely untenable. In any event, the

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amount was not expended in the year of account ending with December 31, 1951 : it was expended in 1948.

It remains to consider the case under s. 10(2)(xi). In this connection, we were referred to the Memorandum of Association to show that it was one of the objects of the assessee company to promote other companies and this amount was paid to Southern Agencies Ltd. to promote the Rodier Textile Mills Ltd. There is no doubt that the objects mentioned in the Memorandum of Association of the assessee company include the promotion and financing of other companies. A Memorandum, however, is not conclusive as to the real nature of a transaction. That nature has to be deduced not from the Memorandum but from the circumstances in which the transaction took place. Here, the different versions given in the books of account of the assessee company belie the assertion that this was an amount paid to promote the Rodier Textile Mills Ltd. Even though this money was available on December 31, 1948, and the subscription list for the shares remained open from January 5 to 20, 1949, no application for a single share was made on behalf of the assessee company. The entry till the end of 1949 was that the amount was laid out for purchase of shares. It was only subsequently that it was shown to be an advance to the Southern Agencies Ltd. In fact, the entry comes only at the end of 1950 when it is set down "By Amount paid to Southern Agencies Ltd."

The assessee company raised three contentions in support of the case that this became a bad and doubtful debt which was actually written off : (a) that the High Court was wrong in saying that before the assessee could claim the deduction under s. 10(2)(xi) it must prove that it had in the past purchased and sold agencies, (b) that the object of the assessee company was to apply for shares but as it did not

apply for shares the transaction between it and the Southern Agencies remained an advance in the ordinary course of business, and (c) Southern Agencies having failed to give back the money the assessee company was within its rights to write off this bad and doubtful debt.

Now, a question under s. 10(2)(xi) can only arise if there is a bad or doubtful debt. Before a debt can become bad or doubtful it must first be a debt. What is meant by debt in this connection was laid down by Rowlatt, J., in *Curtis* v. *J. & G. Oldfield Ltd.*,(1) at p. 330 as follows :—

> "When the Rule speaks of a bad debt it means a debt which is a debt that would have come into the balance sheet as a trading debt in the trade that is in question and that it is bad. It does not really mean any bad debt which, when it was a good debt, would not have come in to swell the profits."

A debt in such cases is an outstanding which if recovered would have swelled the profits. It is not money handed over to someone for purchasing a thing which that person has failed to return even though no purchase was made. In the section a debt means something more than a mere advance. It means something which is related to business or results from it. To be claimable as a bad or doubtful debt it must first be shown as a proper debt. The observations of Rowlatt, J., were applied by the Privy Council in *Arunachalam Chettiar* v. *Commissioner of Income-tax*(2), at p. 245, where their Lordships observed as follows :—

> "Their Lordships moreover can give no countenance to a suggestion that upon a dissolution of partnership a partner's share of the losses for several preceding years can be accumulated and thrown into the scale against

(1) (1925) 9 Tax Cas. 319, 330. (2) (1936) L. R. 63 I. A. 233, 245

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the income of another partner for a particular year. No principle of writing off a bad debt could justify such a course, whether in the year following the dissolution or, as logic would permit, in some subsequent year in which the partner's insolvency has crystallised. The "bad debt" would not, if good, have come in to swell the taxable profits of the other partner."

This Court also approved the dictum of Rowlatt, J., in *Commissioner of Income-tax* v. *Abdullabhai Abdulkadar* (1) at p. 550 and referred to the observations of Venkatarama Ayyar, J., in *Badridas Daga* v. *Commissioner of Income-tax*, (2) where the learned Judge speaking for this Court said that a business debt "springs directly from the carrying on of the business and is incidental to it and not any loss sustained by the assessee, even if it has some connection with his business." Section 10(2)(xi) is in two parts. One part deals with an assessee who carries on the business of a banker or money-lender. Another part deals with business other than the aforesaid. Since this was not a loan by a banker or money-lender, the debt to be a debt proper had to be one which if good would have swelled the taxable profits.

Applying these tests, it is quite obvious that an advance paid by the assessee company to another to purchase the shares cannot be said to be incidental to the trading activities of the assessee company. It was more in the nature of a price paid in advance for the shares which the Southern Agencies had a right to allot in the Rodier Textile Mills Ltd. This cannot, therefore, be described as a debt and indeed the changes in the books of account of the assessee company clearly show that the assessee company itself was altering the entries to convert the advance into a debt so as to be able to write it off and claim

(1) [1961] 2 S. C. R. 949,954. (2) [1959] S. C. R. 590.

the benefit of s. 10 (2) (xi). In our opinion, s. 10(2)(xi) was inapplicable to the facts of this case. In the result the appeal must fail and it is dismissed. The assessee company shall pay the costs of the respondent.

Appeal dismissed.

O. K. GHOSH AND ANOTHER

v.

E. X. JOSEPH

(B. P. SINHA, C. J., P. B. GAJENDRAGADKAR, K. N. WANCHOO, K. C. DAS GUPTA and J. C. SHAH, JJ.)

Services Rules—Association of non-Gazetted civil staff—Withdrawal of recognition by Government—Proceedings against Secretary for refusal to dissociate—Participation in preparation for strike—Constitutional Validity of Rules—Central Civil Services (Conduct) Rules, 1955, rr. 4(A), 4(B)—Constitution of India, Art. 19.

The respondent, a Central Government servant, who was the Secretary of the Civil Accounts Association of non-Gazetted Staff, was departmentally proceeded against under rr. 4(A) and 4(B) of the Central Civil Services (Conduct) Rules, 1955, for participating in demonstrations in preparation of a general strike of Central Government employees and for refusing to dissociate from the Association after the Government had withdrawn its recognition of it. He impugned the validity of the said rules on the ground that they infringed his fundamental rights under Art. 19 of the Constitution. The High Court held that r. 4(A) was wholly valid but quashed the proceeding under r. 4(B) which it held to be invalid. Rule 4(A) provided that no Government servant shall participate in any demonstration or resort to any form of strike in connection with any matter pertaining to his conditions of service and r. 4(B) provided that no Government servant shall join or continue to be a member of any services Association which the