
(1981) 07 MAD CK 0050
In the Madras High Court
Case No : Tax Case No. 620 of 1975

Ghansham Singh

APPELLANT

Vs

Commissioner of Income Tax

RESPONDENT

Date of Decision : 10-07-1981

Acts Referred:

Constitution of India, 1950 — Article 134A
Income Tax Act, 1961 — Section 10(2)(xv), 261

Citation : (1983) 14 TAXMAN 428

Hon'ble Judges : V. Balasubrahmanyam, J;Sethuraman, J

Bench : Division Bench

Advocate : T.V. Ramanathan, for the Appellant; J. Jayaraman and Mrs. Nalini Chidambaram, for the Respondent

Judgement

V. Balasubrahmanyam, J.—This reference from the Tribunal raises the perennial question of capital versus revenue expenditure. We may clear the ground first by excluding from our consideration lines of inquiry on which the indications are that they are unnecessary for the purposes of the present case. We are not, for instance, asked to examine whether the expenditure in question was incurred for the enduring benefit of the assessee's trade. Nor is there any question of the expenditure going into the purchase by the assessee of a fixed capital asset. This is also not a case of an outlay for the acquisition of a business as a whole, nor even of the extension or substantial improvement of an existing business. The deduction claimed is in respect of a payment made by the assessee under the terms of a compromise decree. The compromise came about this way. The assessee was a partner in a partnership concern carrying on commission business and engaged in other sundry activities. With the death of one of the assessee's co-partners, the firm dissolved. The dissolution was by agreement between the surviving partners and the heirs of the deceased partner. Under the agreed scheme of dissolution, the assessee took over the partnership business, lock, stock and barrel, as a going concern, paying a certain sum of money to the deceased's heirs, by way of purchase of their interests in the partnership assets.

After the take over, the assessee carried on business for a time as its sole proprietor. He then converted the business into a partnership, taking his son as a partner. This happened after an interval of five years. At this stage, the assessee was faced with a suit instituted by some of the minor sons of the deceased partner of the erstwhile partnership. The plaintiffs in the suit made all kinds of allegations against the assessee, including an allegation of fraud in the settlement of the accounts. They, accordingly, prayed for the reopening of the earlier dissolution, as a primary relief in the suit. They also asked for an injunction restraining the assessee and his son from carrying on the business as present day partners. As might only be expected, the assessee resisted the suit, denying the allegations of fraud levelled against him. There was, however, no occasion to know on which side the truth lay, for the suit ended in a compromise and a decree was passed by consent of parties. Under its terms, the plaintiff withdrew all their allegations, and the assessee agreed to pay them Rs. 40,000 in full settlement. The assessee paid the money in due time. In this assessment for the relevant account year, the assessee claimed the payment of Rs. 40,000 as an admissible deduction. The ITO, however, disallowed the expenditure. The officer's view was that the deduction was asked for in the father and son partnership, whereas its subject-matter related to an earlier, but now defunct, partnership. A different view, however, was taken by the AAC on appeal. He held that since the assessee was being taxed in respect of his share income from the business in which he was a partner along with his son, he was entitled to set off the payment of Rs. 40,000 as against that share income. The department, however, appealed against this determination of the AAC. The Tribunal allowed the department's appeal. The Tribunal took the view that the payment made by the assessee to the heirs of the deceased partner in the erstwhile partnership was capital expenditure. On this single ground, the Tribunal disallowed the expenditure.

2. The assessee then asked for a reference to the Court. The Tribunal obliged, and stated a case on the following question:

Whether, on the facts and in the circumstances of the case, the Tribunal was right in law in holding that a sum of Rs. 40,000 paid to the sons of Sri Kuppuswami Naicker was a capital expenditure and not deductible in determining the income of the assessee?

3. To answer this question, it would be necessary to find out on what basis the Tribunal had rejected the assessee's claim that the payment in question was an item of revenue expenditure. The assessee had urged before the Tribunal that the payment was made only to preserve and protect the business which was being run by the assessee in partnership with his son from the onslaught of the plaintiffs who were insistent on raking up a settlement, made five years earlier, under which the assessee had obtained full title to the business. The Tribunal rejected the basic idea behind this contention by holding that under the law expenditure incurred by an assessee to protect his business would be capital

expenditure and not revenue expenditure.

4. The Tribunal's view of the law is, in our judgment, incorrect. The Supreme Court have laid down that expenditure to protect an assessee's trade or to maintain his business is not capital expenditure, but allowable as an item of revenue expenditure. This enunciation of the law is to be found in the following passage in the Supreme Court's judgment in *Dalmia Jain and Co. Ltd. Vs. Commissioner of Income Tax, Bihar, Orissa and Patna*, :.

...The principle which has to be deduced from decided cases is that, where the expenditure laid out for the acquisition or improvement of a fixed capital asset is attributable to capital, it is a capital expenditure but if it is incurred to protect the trade or business of the assessee then it is a revenue expenditure. In deciding whether a particular expenditure is capital or revenue in nature, what the Courts have to see is whether the expenditure in question was incurred to create any new asset or was incurred for maintaining the business of the company. If it is the former it is the capital expenditure; if it is the latter, it is the revenue expenditure.

5. Although the Supreme Court deduced the above principle from "decided cases", they did not proceed to refer to any of them. Apparently, the Court thought they did not have to give the citations, as the law was well settled. We may, however, observe, with respect, that the Supreme Court's reference to "decided cases" is borne out by a study of the case law on the subject, especially that which obtains in England.

6. The best known enunciation of the principle that a payment made by a taxpayer to protect his trade is a revenue item of expenditure is that of Lawrence, J., in *Southern v. Borax Consolidated Ltd.* (1942) 10 ITR (Suppl.) 1 (KB). In the case before Lawrence, J., the payment, briefly stated, was made under a compromise of an action concerning a piece of land. The action had been filed, challenging the title of the taxpayer to the property. With the payment under the compromise, the suit was apparently not pressed. The learned Judge pointed out that the payment of money to the plaintiff in the action and other legal expenses did not create any new asset, but were expenses incurred in the ordinary course of business to maintain the taxpayer's title to the property. In the course of his judgment, the learned Judge drew a clear distinction between expenditure laid out for the acquisition or improvement of a fixed capital equipment, on the one hand, and expenditure incurred for maintaining that asset, on the other. The former, he said, must be attributed to capital; and the latter, being a mere matter of maintenance, must be attributed, according to him, only to revenue.

7. The validity of Lawrence, J.'s distinction has never been doubted in later English decisions, but has been affirmed, time and again. In the case of *Associated Portland Cement Mfrs. Ltd. v. Kerr (Inspector of Taxes)* (1946) 27 TC 103 (CA) for instance, Macnaghten, J., brought out the crux of the decision of

Lawrence, J., in *Borax's case* (supra) in the following passage:

The Borax company owned some real property abroad and it had to incur legal expenses in defending its title to the property, and the question was whether those expenses should be treated as income or as capital expenses; on that question there could, I think, be little doubt but that they were to be regarded as expenses properly chargeable to income.

8. A similar view was expressed by Lord Greene, M.R., in the case of *Associated Portland Cement* (supra) when it came up before the Court of Appeal. The learned master of the Rolls summarised the point of distinction laid down in *Borax's case* (supra) thus:

The money that you spend in defending your title to a capital asset, which is assailed unjustly, is obviously a revenue expenditure. There, again, there is all the difference in the world between defending your assets against the claim of somebody who has no claim against them, and acquiring a new asset or adding to an existing asset.

9. In a later case, *Cooke (Inspector of Taxes) v. Quick Shoe Repair Service* (1949) 30 TC 460, a similar question arose. A shoe-repair business was purchased by the taxpayer from another person. Under the purchase, it was the responsibility of the vendor to discharge all outstanding liabilities of the business, as on the date of the sale. The vendor, however, failed to do so. In the event, the taxpayer, as purchaser of the business, had to pay certain sums in discharge of the vendor's liabilities. This was done solely with a view to preserve the goodwill of the shoe-repair business and to ensure to the taxpayer continuity of supplies of raw material and the like. Having discharged these liabilities, the taxpayer company claimed the outgoings as revenue expenditure. It was held that the expenditure was allowable as having been made on revenue account. *Cruom-Johnson, J.*, who decided this case, referred to *Borax's case* (supra) and other earlier cases and culled out their principle in the following terms:

The cases show that, if money is expended with a view to preserving an asset, the result of it is, once the Commissioners are satisfied of that circumstance, it may be deductible expenditure.

10. In *IRC v. Carron Co.* (1967) 45 TC 18 (HL) , which is a case from Scotland, the taxpayer company was carrying on the business of iron-founders under a Royal Charter of 1773. By the 1950s, many of the company's features had become archaic and unsuitable to modern industrial conditions. In consequence, the company's production was suffering from a progressive decline. They then applied for a revision of the charter and incurred expenditure in that connection. Subsequently, the company claimed the expenditure as revenue expenditure in the computation of the company's annual profits and gains chargeable to income tax. In the case stated, the Commissioners for the special purposes specifically stated : "We could not see any new capital asset." On that basis, they concluded that the expenditure was revenue expenditure and allowable. On the case stated,

the Court of Session of Scotland held that the object of the new charter was to remove obstacles to profitable trading and, hence, the expenditure was on income account. Lord Cameron, one of the members of the Court of Session, put it on the ground that the expenditure was for maintenance of the taxpayer's business. He expanded the concept of maintenance expenditure with the following picturesque observations:

The advantages to be gained were directed specifically to the existing business activities of the company, and the payments to settle the pending litigation were the price of removing grit which caused, and could cause, unacceptable failure in the company's machinery. The trading machinery required repair and modernising-this was the purpose of the expenditure.

11. The House of Lords agreed with the decision of the Court of Session and held that the expenditure was on revenue account. Lord Guest, in the House of Lords, adopted the imagery of Lord Cameron that the expenditure incurred in obtaining the supplementary charter was to repair the business machinery and to remove the grit which could cause failure to that machinery. Lord Wilberforce in the same appeal particularly referred to the finding of the Special Commissioners that they "could not see any new capital asset", and regarded this finding as significant.

12. Borax's case (supra) was decided by Lawrence, J., in 1940. Carron Co.'s case (supra) was decided by the House of Lords in 1968. In between arose the other cases we have mentioned. English text-book writers have referred to the payments which have figured in these cases, as "protection money payments". Throughout the period of three decades or four, after Borax's case (supra) was rendered, there has not been one case in which any Court had held that protection money laid out to protect or maintain a tax payer's business is capital expenditure. In case after case the position was reiterated that it was revenue expenditure. In case after case, it was pointed out that only expenditure for acquisition of, and improvement to, the business would be capital expenditure. Our Supreme Court, with respect, was, accordingly, quite correct in observing, in Dalmia Jain's case (supra), that the distinction between the two types of expenditure with two different objections must be regarded as quite well settled.

13. We may now briefly refer to the facts in Dalmia Jain's case (supra). We do so for a better understanding of the principle laid down therein. In the case before the Supreme Court also, as in the instant case, the payment made by the assessee was in the nature of protection expenditure for protecting or maintaining the assessee's business. In that case a lease of Government lands for quarrying limestone for a period of twenty years was promised by the State of Bihar to a mining company. Owing to some previously instituted litigation by a third party, the State Government did not deliver possession to the mining company. After the lands came under the Government's possession, they directly appointed the assessee as their agent for working the quarry. The mining company then filed a suit for specific performance of the agreement for lease. They impleaded both the State Government and the assessee as party-

defendants. After the suit was disposed of, but by the time a final decision could be rendered in appeal, the period of twenty years itself had expired. With the result that instead of a decree for specific performance in its favour, the mining company was awarded damages. The assessee was liable under the appellate decree to pay a portion of the damages. The assessee paid the amount. In its assessment to income tax, the assessee claimed the payment as an item of revenue outgoing. The Supreme Court upheld the assessee's claim. The Court pointed out that at the time of the litigation, the assessee was carrying on the quarry business. The Court observed that the assessee did not get into the litigation of its own accord, but was dragged into it by the mining company. In these events, the Supreme Court held that the payment was made only to protect the assessee's business. It only remained for the Supreme Court thereafter to apply the principle, which, as they rightly observed, could be "deduced from the decided cases", and render their decision in that case to the effect that expenditure incurred to protect the trade or business of the assessee was revenue expenditure.

14. The Tribunal, however, were apparently unaware of this ruling of the Supreme Court in *Dalmia Jain's case* (supra). There is no knowing whether they knew about the catena of English decisions on expenditure of this kind in which the destruction had been clearly marked. They relied, instead, on an observation to be found in an earlier Supreme Court case in *V. Jaganmohan Rao and Others Vs. Commissioner of Income Tax and Excess Profits Tax, Andhra Pradesh*, to support quite the opposite conclusion, namely, that expenditure on perfecting the title to one's business is only capital expenditure. The passage on which the Tribunal placed reliance was as follows:

...It is well established that where money is paid to perfect a title or as consideration for getting rid of a defect in the title or a threat of litigation the payment would be capital payment and not revenue payment....

15. Although the proposition which had been given expression to in the above passage is found described, with confidence, as "well settled", the judgment of the Supreme Court does not refer to any authorities, English or Indian, in which that proposition was either enunciated or reiterated. We would give anything to know that were the decided cases which according to the Supreme Court, had settled the doctrine that an expenditure to perfect the title to a capital asset is capital expenditure. For, as we have earlier shown, in addition to the authority of our own Supreme Court in *Dalmia Jain's case* (supra), there are as many as four direct decisions of the English Courts, in an unbroken span of four decades, which have laid down quite the opposite principle as governing the allowance of expenditure to protect the title to a business or other fixed capital asset of a businessman. The Supreme Court's observation in the case of *V. Jaganmohan Rao's case* (supra) would thus seem to be a stray observation, and a mere obiter dictum. This aspect of the decision needs to be elaborated upon. The issue before the Supreme Court in this case was concerned with the question of

allowance of expenditure which was incurred, not for the protection or maintenance of the title of an assessee to a business or a fixed capital asset of his, but for the very acquisition of the fixed capital asset. The facts relied on by the Supreme Court showed that the assessee in that case had purchased an item of land from the father of two minor sons, while there was a suit for partition which was even then pending between the father and the sons. In that suit, the ownership of that property was contested and was a fact in issue. The claim of the father was that the property was his self-acquisition. It was the case of the sons that it belonged to the joint family and, hence, they too were entitled to their shares in the property. The Court of first instance held that the property was the self-acquisition of the assessee's vendor and not joint family property in which the vendor's sons had any right by birth. On appeal, the High Court disagreed with that finding. The assessee was a party-defendant to the proceedings. That being so, he preferred an appeal to the Privy Council. Pending the appeal, however, he took counsel and entered into a compromise with the two minor sons. Under the terms of the compromise, the assessee paid them Rs. 1,15,000 and obtained a release of their claims against the property. Meanwhile, the assessee was himself appointed by the Court as a receiver of the property. As receiver, the assessee was collecting the rents and profits from the property. Ultimately, the Privy Council decided the appeal in the assessee's favour. They held that the assessee's vendor had absolute and exclusive title to the property. In his assessments to income tax for the relevant years, the assessee offered the rents and profits which he received from the property as a receiver. He, however, set against those receipts the amount of Rs. 1,15,000 which he paid to the sons of his vendor by way of compromise of their claims. On reference, the Supreme Court posed the question for their consideration as follows:

What is essential to be seen is whether the amount of Rs. 1,15,000 was paid for bringing into existence a right or asset of an enduring nature. In other words, if the asset which is acquired is in its character a capital asset, then any sum paid to acquire it must surely be capital outlay.

They then gave answer to the question posed in the -following terms:

It was a lump sum payment for acquisition of a capital asset and the claim of the plaintiffs, for the lease money from the property was merely ancillary or incidental to the claim to the capital asset.

16. Dalmia Jain's case (supra) was decided by a Bench of two Judges of the Supreme Court, whereas the Bench which decided the case of V. Jaganmohan Rao's case (supra) consisted of three Judges. We have seen now that there is a conflict between these two cases. What are we to do in a situation of this kind?

17. Normally the rule is that where the law is laid down differently in two different decisions of the Supreme Court by Benches of different strength, the decision of the larger Bench shall be followed as the binding decision on the subject. A further rule of practice is that even the Supreme Court's obiter dicta

are binding on this Court. Although these are the normal rules of stare decisis as applied to Supreme Court's decisions, we think we would be justified in regarding Dalmia Jain's case (supra), as authoritative and binding as the ruling decision for purposes of our present case. We believe that the doctrine that a larger Bench of the Supreme Court has more authoritative force than a smaller Bench is only relevant as between cases which yield different ratios decidendi, and not where the one hands down a decision and the other merely lays down a dictum. In this case, the dictum in V. Jaganmohan Rao's case (supra) is not only obiter, but it has been rendered, with respect, per incuriam. This Bench of three Judges, apparently, had not been duly appraised of the trend of decisions in Borax's case (supra), in Associated Portland Cement's case (supra), in Quick Shoe's case (supra) and in Canon's case (supra). If they had known about these cases, and had considered the principle laid down in unbroken uniformity in all of them, we dare say the Court would have given expression to the same proposition which the Court happened to lay down only two years later in Dalmia Jain's case (supra). As between a decision which is per curiam and a decision which is per incuriam there can be little or no doubt as to where our duty lies as a Court bound by the doctrine of stare decisis and the decisions of the Supreme Court. We are, accordingly, satisfied that the Tribunal's decision in this case, although based on a dictum of the Supreme Court in V. Jaganmohan Rao's case (supra), must be held to be erroneous since it is opposed to the law laid down directly on the point by the subsequent Supreme Court decision in Dalmia Jain's case (supra).

18. We may, however, observe, in passing, that the distinction laid down by Lawrence, J., in Borax's case (supra) had not been accepted, without question, in Australian Courts administering more or less similar legislation on income tax—Sun Newspapers Ltd. v. Federal Commissioner of Taxation (1938) 61 CLR 337. In this case Dixon, J., in the High Court of Australia, expressed the notion that money paid by a taxpayer with a view to preserve his existing business organization from immediate impairment and dislocation is an outgoing of capital and, hence, not deductible in the computation of taxable business income. For a similar view, see also Booken Hill Theatres Proprietary Ltd. v. Federal Commissioner of Taxation (1952) 85 CLR 423, a decision of the full Court, in which Lawrence, J.'s decision in Borax's case (supra) was doubted. The views of Australian Judges, however, do not seem to be uniform. And more recent trends in judicial pronouncements in that country show a change in emphasis. See, for instance, the observations of Latham, C.J., in Hallstombs Proprietary Ltd. v. Federal Commissioner of Taxation (1953) 72 CLR 634 and of Taylor, J., in Federal Commissioner of Taxation v. Duro Travel Goods Proprietary Ltd. (1946) 87 CLR 524.

19. It might well be that Borax's case (supra) does not carry the unquestioned authority it once had. The mark of distinction laid down in that case between expenditure to purchase a fixed capital asset, on the one hand, and expenditure to protect the same asset, on the other, might be thought to require

reconsideration in the light, at any rate, of the trend of Australian judicial opinion. But till that time arrives, we believe we would be justified in following Dalmia Jain's case (supra) as the ruling decision on the subject.

20. The Tribunal in their order have found all the material facts to which we have refer red in the beginning of this judgment. They have adversed to the original partnership; its subsequent dissolution, on the death of the assessee's co-partner, the take over of the business and the purchase of the deceased's share by the assessee by payment to his heirs; the subsequent running of the business as the, assessee's sole proprietary concern; the assessee's conversion of the business, after a five-year lapse of time, as a father-and-son partnership; the suit filed by the minor children of the deceased partner of the erstwhile partnership, the compromise of the suit and the payment of the amount to the deceased's heirs and the withdrawal of the suit. The Tribunal, after referring to all these facts, asserted that the assessee had not acquired full title to the business at the time of the dissolution of the old partnership, but acquired it only when it paid Rs. 40,000 under the compromise. The Tribunal relied on the plaint allegations in the suit to reach the conclusion that prior to the compromise decree the assessee's title to the business, although paid for under the scheme of dissolution, was imperfect.

21. There is, in our judgment, no warrant for this conclusion. The plaint in a suit could by no means, be relied on as a record of facts.-"It is but a pleading. The plaint allegations have stood denied in this case by the assessee's written statement. What is more, both parties to the litigation had given the go-by to their respective pleadings, when they entered into a mutual compromise. There is nothing express or implied in the terms of the compromise to suggest that the payment of Rs. 40,000 to the heirs of the deceased partner was towards payment of the balance of the purchase price of the deceased partner's share in the business. In these events, it would be safe and reasonable to hold that so far as the assessee was concerned, the suit was an attack on the title to his business, and so far as his payment of Rs. 40,000 was concerned, the payment warded off that attack. The Tribunal was not justified in assuming that the payment under the compromise decree was the means by which the assessee had acquired full title to the business. The situation presented by this case is quite different from that which obtained in V. Jaganmohan Rao's case (supra) but is almost parallel to the fact situations found in Borax's case (supra) and Dalmia Jain's case (supra).

22. One aspect of the case which the Tribunal had overlooked while disposing of the appeal before them, needs to be briefly touched upon. As earlier mentioned, the ITO had disallowed the allowance claimed by the assessee for Rs. 40,000, in the year of payment, the officer's reason, as already mentioned, was that the liability related back to the business at a time when it was run as the sole proprietary concern of the assessee, and not at the material tune when it had become a father-and-son partnership. The AAC had rejected this approach of the

ITO to the question of allowability of business expenditure. He held that since the assessee's share income from the father-son partnership was to be charged to tax as business income, it was permissible to set against it any outgoing properly debitable to revenue.

It was precisely this aspect of the decision of the AAC which was, questioned by the department in their appeal before the Tribunal. But the Tribunal did not deal with the question, they proceeded instead, to dispose of the department's appeal on the other issue as to whether the payment of Rs. 40,000 was capital or revenue expenditure. It is, therefore, no wonder that the question of law referred to us also pinpoints only the capital versus revenue feature of the controversy. Yet, for the sake of completeness of the discussion, we would face the controversy whether the payment of Rs. 40,000 could at all be considered in the context of the assessment of the assessee's share income from the present firm, when, in terms of its history, the payment relates to a previous period of proprietary ownership of the business.

23. When a partnership carries on a business, every partner thereof must be regarded as carrying it on, although he does so only in co-partnership with the other partners. See the observations of Raghava Rao, J., in *The Commissioner of Income Tax, Madras Vs. S.V.R.N. Palaniappa Chettiar (died) and Others*, . It is on the basis of this fundamental conception of partnership that we have a long line of cases in which it has been decided that the share of income of a partner from a partnership firm must be brought to charge as profits under the head "Business". The Courts have further held that as against that share income the partner would be entitled to set off all legitimate items of expenditure which may be regarded as admissible by the application of principles of commercial accounting. In the present case, the assessee had all along been carrying on business, first as a partner along with three other individuals, next on the dissolution of the partnership by death of one of the other partners, as sole proprietor for five years, and thereafter, in partnership with his son. All throughout, the business was the same. There were differences only in the persons carrying on the business at different periods of time. In the year of account relevant to the assessment year under reference, the assessee was but a partner and his income from the business was but a share income from that firm, the other share being that of his son. The assessee, however, is not thereby disentitled to claim set off of legitimate expenditure which appertains to that share income. The department's case had always been that the payment of Rs. 40,000 made by the assessee did relate to the business because it was that business which the assessee had taken over from the partnership business and it was that business which was the subject-matter of the law suit by the heirs of the deceased partner. If so much is granted, we see no reason why the deduction in question cannot be attributed to that business. The AAC dealt with this point when he decided that the payment of Rs. 40,000 by the assessee would be a proper set off as against the share income of the assessee from the firm. We are in entire agreement with this view.

24. It was pointed out in argument by the department's learned counsel that the sum of Rs. 40,000 as an outgoing, was found debited, not in the partnership accounts, but in the books separately kept for certain money-lending transactions of the assessee. One reason for not recording the expenditure in the account books of the father-and-son partnership might be that, historically, the entire liability was that of the assessee alone. What ever might be the reason for not setting off the outgoing against the profits, or the assessee's share of profits, in the firm's books, it is understandable that the expenditure has a nexus only to the business which was being carried on by the assessee both as proprietor and as a partner at various stages. The question for consideration is not where, and in which accounts, the expenditure is found debited, but whether the expenditure is relatable to the business. To this latter question, the facts found provide a complete answer in the assessee's favour.

25. The result is that we must decide the question of law in this reference in the negative and against the revenue. We hold, in short, that the sum of Rs. 40,000 paid by the assessee to the sons of the deceased partner, is not capital expenditure, but is a revenue item of outgoing liable to be allowed while determining the assessee's income under the head "Business" for the concerned assessment year. The assessee will have the costs of this reference from the department. Counsel's fee Rs. 500.

Sethuraman, J.

26. Before going through the judgment prepared by my learned brother, I had prepared my own and after going through the detailed discussion of the legal principles, I would now content myself with expressing my concurrence with the answer proposed to the question for the reasons indicated below. Just to make my judgment clear, I would state the facts first.

The Madras Electric Tramway Co. Ltd. was brought into liquidation under the supervision of this Court. It had lands, tramway tracks and overhead wires, which were advertised for sale. Kuppuswami Naicker made a tender to the official liquidator for purchasing these assets for a sum of Rs. 5,51,111. The tender was accepted on 19-8-1955. Kuppuswami Naicker was unable to pay the money. An assignment of the contract in favour of Sri Bhagwan Motor Co. came into existence under a document dated 16-3-1955. The firm consisted of Kuppuswami Naicker, his son P.K. Ramadoss, Mohanlal Lekhranjmal and the assessee Ghansham Singh, who died on 12-1-1971. The firm deposited the amount due under the contract. There were disputes between the firm on the one hand and the Corporation of Madras on the other with regard to the removal of tramway rails, overhead materials, etc., and to the restoration of the roads to their original condition. It appears that Kuppuswami Naicker himself had expressed a desire that the firm should be dissolved and the business should be carried on by the assessee solely, as he had contributed the necessary finances. Before anything could be done in this behalf, Kuppuswami Naicker died on 15-11-1955. The result was that the partnership became dissolved. On 25-11-1955, the remaining

partners entered into a deed of dissolution under which the widows of Kuppuswami Naicker were paid Rs. 37,000 and his two minor sons Rs. 26,000. Thereafter, the business was carried on by the assessee as the sole proprietor till 18-10-1960. With effect from 19-10-1960, he took his son as the working partner with one-third share.

27. Four of the sons of Kuppuswami Naicker, of whom three were minors, instituted C.S. No. 3 of 1960 in the original side of this Court, praying for setting aside the deed of dissolution and directing the assessee to render a full and completed account of the partnership and its assets. The suit was contested by the assessee. Ultimately, it ended in a compromise. A memo of compromise was entered into on 7-9-1962, under which the assessee had to deposit into Court a sum of Rs. 40,000 to be paid to the plaintiffs in the suit in full quit of their claim. As some of the plaintiffs were minors, the High Court accorded sanction to the said compromise being entered into.

28. This sum of Rs. 40,000 paid to the sons of Kuppuswami Naicker was claimed as expenditure allowable under the Act. The assessee continued to be a partner in the firm, which came into existence on 19-10-1960. The assessment year under consideration is 1964-65, the relevant previous year ending on 17-10-1963. The ITO rejected the claim, but it was allowed by the AAC. At the instance of the department, there was an appeal to the Tribunal, which reversed the order of the Assistant Commissioner and restored that of the ITO. The consequence was that the sum of Rs. 40,000 stood disallowed in the assessment. The following question has been referred:

Whether, on the facts and in the circumstances of the case, the Tribunal was right in law in holding that the sum of Rs. 40,000 paid to the sons of Kuppuswami Naicker was a capital expenditure and not deductible in determining the income of the assessee?

29. The Tribunal has mainly based its judgment on a decision of the Supreme Court in V. Jaganmohan Rao's case (supra). In that case, there was already a pending litigation between the father and the sons. While the father claimed that a spinning mill and other properties were his individual properties, the sons contended that they were joint family properties. They filed a suit for partition. The trial Court dismissed the suit. When the appeal was pending, the mill was sold by the father to the assessee. In the appeal, against the dismissal of the suit, it was held that the properties were not the self-acquired properties, but were joint family properties in which the plaintiffs had a two-third share. The father filed an appeal before the Privy Council. When the matter was pending there, there was a compromise under which the assessee, the purchaser of the mill, paid a sum of Rs. 1,15,000 to the two sons and got a release of their interest in the mills. This amount was claimed as deduction in the assessment of the assessee. The High Court held that the amount had been paid for acquisition of the capital assets and that the payment had been made in order to perfect title to the capital asset. The claim for deduction was, therefore, rejected. In the

course of the judgment, it was observed:

...It is well established that where money is paid to perfect a title or as consideration for getting rid of a defect in the title or a threat of litigation the payment would be capital payment and the revenue payment....

30. This is not a case where the assessee is trying to perfect his title to the property, as it happened in the case before the Supreme Court. This is a case where the assessee had acquired title to the assets even at the time when he originally entered into partnership with Kuppuswami Naicker. Under the deed of dissolution, he became the sole owner of the assets of the partnership. Whatever consideration was payable for the assets had already been paid and the amount now under consideration is not part of the said amount. If the suit had not been filed by the sons of Kuppuswami Naicker, there was no necessity for the assessee to go to the Court to perfect his title. In the case before the Supreme Court, the assessee had to make a payment for getting rid of a defect in title. In fact, he purchased the assets at a time when the title to the property purchased was under challenge. The same is not the position here.

31. Courts in India have accepted the principle of the decision of the King's Bench Division in *Borax's* case (supra). The principle laid down in that case has been stated in the following words:

On the other question as to whether this is a payment properly attributable to capital or to revenue, in my opinion the principle which is to be deducted from the cases is that where a sum of money is laid out for the acquisition or the improvement of a fixed capital it is attributable to capital, but that if no alteration is made in the fixed capital asset by the payment, then it is properly attributable to revenue, being in substance a matter of maintenance, the maintenance of the capital structure or the capital assets of the company....

In that case, a British company had taken over an Island in California. The city of Los Angeles commenced an action in the United States claiming that the British company's title to the land and buildings was invalid and that such land and buildings were in fact the property of the city of Los Angeles. This action was defended by the British company, and in so doing it incurred expenditure, which was claimed deduction in the income tax assessment. It was held that the amount was allowable as deduction. It was pointed out that the only way in which it can be said that there was any alteration in the capital assets of *Borax Consolidated Ltd.*, was that the city of Los Angeles had been removed from the category of possible litigants who might challenge the company's title and that it did not make the payment a capital payment. The title of the company, which must be assumed to have been a good title remained the same; there was nothing added to the title or taken away from it and the title had simply been maintained by this payment.

32. This decision was distinguished in *Selvarajulu Chetty & Co. (India) v. CIT* (1966) 56 ITR 29 (Mad.). That was a case where the dispute related to the title

to the business, in its entirety and the question was whether on the death of the previous owner it had vested on his daughter or on certain other relations. The expenses in such a litigation were considered to be outside the scope of allowance and Borax's case (supra) was found to be hardly in point. It was pointed out:

...If a sum of money is expended for the acquisition or the improvement of a fixed capital asset, it is undoubtedly attributed to capital. But if there is no change in the fixed capital asset, then the expenditure is properly attributable to revenue....

33. The Supreme Court has considered the principle applicable to cases of this kind in two later decisions. The first of them is *Shree Meenakshi Mills Ltd., Madurai Vs. Commissioner of Income Tax, Madras*, . In that case, a spinning mill distributed the yarn produced by it to the weavers outside the factory. The Textile Commissioner issued an order directing that the company should not so sell or deliver yarn manufactured by it, except to such person or persons as he may specify. The mill challenged the validity of this order in this Court, and ultimately took the dispute to the Privy Council. It failed in the litigation. The expenditure incurred by it was claimed as deduction. Shah, J., as he then was, delivering the judgment of the Supreme Court pointed out:

...Expenditure on civil litigation commenced or carried on by an assessee for protecting the business is admissible as expenditure u/s 10(2)(xv) provided other conditions are fulfilled, even though the expenditure does not directly relate to the earning of income...

Earlier at page 212 it was pointed out that the expenditure incurred in prosecuting a civil proceeding relating to the business of an assessee is admissible as expenditure laid out wholly and exclusively for the purpose of the business even if the proceeding is decided against the assessee.

34. In the second case *Commissioner of Income Tax, West Bengal I Vs. Birla Cotton Spinning and Weaving Mills Ltd.*, the assessee claimed deduction of expenditure incurred in contesting certain proceedings before the Investigation Commission and also in Courts, where the vires of the statute under which the Commission was constituted were challenged. It was held that the expenses were liable to be allowed as deduction and it was observed:

The essential test which has to be applied is whether the expenses were incurred for the preservation and protection of the assessee's business from any such process or proceedings which might have resulted in the reduction of its income and profits and whether the same were actually and honestly incurred. It is not possible to understand how the expenditure on the proceedings in respect of the Investigation Commission by the assessee will not fall within the above rule....

In *Dalmia Jain's* case (supra) the principle laid down by the Supreme Court was that if the expenses were incurred for the purpose of creating, curing or

completing any title to any property, then it would be capital expenditure, but if they were incurred to protect the business then it must be considered as revenue expenditure.

35. Thus, the authorities uniformly lay down the principle that where the expenditure is incurred for protecting the assets from an attack, then it would be revenue expenditure. It would, however, be capital expenditure if it was incurred for perfecting title or for getting rid of a defect in title. Applying this principle it would be clear that in the present case the assessee had already become the owner of the assets in 1955 and he had to defend the attack on the assets. This is thus clearly a case where the expenditure has not brought into existence any capital asset or enduring benefit.

36. The fact that the expenditure has been incurred at a time when the assessee was only a partner and not sole owner of the assets cannot make a difference, as it is well settled that a person carrying on a business in partnership with another is nonetheless carrying on a business. Another contention urged for the revenue was that the expenditure related to the very framework of the taxpayer's business and was, therefore, capital. It is not possible to accept this submission. The said principle has been evolved in cases where there was a pooling agreement between companies for sharing profits and losses or where money was paid for the cancellation of an agreement which affected the whole structure of the trader's profit-making apparatus. This is a case where after having acquired the assets and carried on business with them, the assessee finds himself involved in a litigation brought out by a third party. In considering the nature of the expenditure, it would not be proper to proceed on the basis of the correctness of the pleadings in the suit, as the matter was not adjudicated upon by the Court. The pleadings represent mere allegations and unless the statements were proved they would merely remain as allegations. So long as there was no adjudication on the conduct of the assessee, the allegations made should not colour the determination of the issue. The principle applicable to cases where a person purchases assets with the knowledge of defect in title and where he subsequently incurs expenditure for perfecting his title, cannot be applied to cases where the assessee had acquired assets and had been carrying on business with them when an attack by some interested person was made. The expenditure had a protective element or a defensive character. Such expenditure would have to be allowed as deduction. Otherwise the assessee would not have been able to keep the assets and earn the profits on which he was taxed. The result is that the question is answered in the negative and in favour of the assessee. The assessee would be entitled to his costs. Counsel's fee Rs. 500.

Sethuraman, J.

When the judgments were pronounced, the learned standing counsel for the Commissioner, Mr. J. Jayaraman, made an oral application for leave to appeal to the Supreme Court in accordance with article 134A of the Constitution of India read with section 261 of the income tax Act, 1961. The question that has been

discussed in the present case is, no doubt, a routine one-of the capital or revenue character of the expenditure. But in the judgment, Balasubrahmanyam, J. has brought out some apparent conflict between the decision of the Supreme Court in V. Jaganmohan Rao's case (supra) and Dalmia Jain's case (supra). In view of the matter having to be authoritatively decided by the Supreme Court, we think it fit to grant leave to appeal to the Supreme Court in the present case. Accordingly, leave is granted.