

(1974) 12 MAD CK 0009

In the Madras High Court

Case No : Tax Case No. 108 of 1969 (Reference No. 24 of 1969)

M.S.P. Raja and Another

APPELLANT

Vs

Commissioner of Income Tax

RESPONDENT

Date of Decision : 19-12-1974

Acts Referred:

Income Tax Act, 1961 — Section 36(1), 67(3)

Citation : (1976) 105 ITR 295

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

Bench : Division Bench

Advocate : S. Swaminathan and K. Ramagopal, for the Appellant; V. Balasubrahmanyam and J. Jayaraman, for the Respondent

Judgement

Sethuraman, J.—This is a reference under the Income Tax Act raising the following question :

Whether, on the facts and in the circumstances of the case, the disallowance of the claim for deduction of interest u/s 36(1)(iii) of the Income Tax

Act, 1961, amounting to Rs. 12,198 or any part thereof in the case of Shri M. S. P. Rajah and Rs. 26,940 or any part thereof in the case of Shri

M. S. P. Rajes is lawful ?

2. The reference is common to two assesseees as the facts in each of these cases are identical. M. S. P. Rajah and M. S. P. Rajes are brothers.

They were partners in two firms known as ""Messrs. M. S. P. Nadar Sons"" and ""Messrs. Hill Tiller and Company"". In September, 1962, that is,

during the financial year 1962-63, the two assesseees constituted another firm called ""Riverdale Estate"", which is said to be an estate raising mainly

coffee in Yercaud. Each of them contributed Rs. 3,00,000 for the purchase of the said agricultural estate. The capital was provided by the two

assess by withdrawal of a like sum from the firm of Messrs. M. S. P. Nadar Sons with which they had a running current account. To the said

account there are debits on account of drawings for personal Income Tax, life insurance premia, etc. While the firm of Messrs. M. S. P. Nadar

Sons gave credit to the two assesseees in regard to the interest on the deposit put in by them, it also charged interest to the assesseees on the

drawings made by them at 9 per cent. per annum. The net result was that M. S. P. Rajah had to pay Rs. 18,236 and M. S. P. Rajes Rs. 33,422 as

interest on the debit balances in their account, as mentioned above. These payments of interest were for the accounting year ended March 31,

1964. The relevant assessment year with which we are now concerned is 1964-65.

3. The two assesseees claimed before the Income Tax Officer deduction for the aforesaid sums of Rs. 18,236 and Rs. 33,422 u/s 36(1)(iii) of the

Income Tax Act, 1961, against their share income from the two partnership concerns, namely, "M. S. P. Nadar Sons" and "Hill Tiller and

Company". The Income Tax Officer allowed a deduction to the extent of certain estimated amounts which, according to him, represented the

allowable deductions under the provision mentioned above. It is not necessary for us to go into the details of the figures given by the Income Tax

Officer because these figures have undergone variation at the successive stages of the appeal before the Appellate Assistant Commissioner and

before the Tribunal.

4. It may be mentioned here that the amounts which remained disallowed as a result of the Tribunal's order are Rs. 12,198 in the case of M. S. P.

Rajah and Rs. 26,940 in the case of M. S. P. Rajes. The figures as such are not in dispute. The disallowance as made by the Income Tax Officer

was on the ground that the withdrawals related to non-business purposes such as purchase of agricultural estate during the financial year 1962-63,

income from which was not assessable to Central Income Tax. The Appellate Assistant Commissioner, on appeal, confirmed the disallowance and

the matter was taken on appeal to the Tribunal.

5. One of the contentions taken before the Tribunal was that the two assesseees were carrying on a single business, that the business was one of

providing capital for the firms in which they became partners and that this

business fell into three compartments of providing capital to the respective firms. It was submitted that though the share income from the firm of "Riverdale Estate" was exempt from the Central Income Tax being agricultural, the income in regard to the borrowed capital provided to the firm of Riverdale Estate was deductible from the share income derived from the two firms. According to the Tribunal no material was placed before it to show that the various activities carried on by the assesseees constituted a single business. It was pointed out that the acts of becoming partners in more than one firm and contributing capital would not constitute a business in itself. The Tribunal observed also that the share income in regard to partnership activity had to be computed separately and that the expenditure relating to one partnership could not be deducted against the profits from the other. The Tribunal held also that the assesseees were carrying on more businesses than one in partnership with others and that these businesses were distinct and separate. As the respective sums of Rs. 3,00,000 with- drawn from the firm of Messrs. M. S. P. Nadar Sons were provided to Riverdale Estate, which produced agricultural income exempt from Central Income Tax, the expenditure relating to such activity had to be completely left out of account. The Tribunal accordingly, held that the interest payable by the assessee on monies borrowed as mentioned above was not a permissible deduction under Section 36(1)(iii).

6. It is as against these conclusions of the Tribunal that the matter has been taken on reference before us.

7. The learned counsel for the assesseees submitted that the view of the Tribunal that because the activity of Riverdale Estate was agricultural, it would justify the disallowance, was erroneous. He contended that so long as the income from investment was liable to be taken into account as income (whether assessable or not) the interest paid for the investment was allowable under the Act. His point was that the agricultural estate represented a business as set and the question as to whether the income from this asset was taxable or (sic) was not at all relevant. In the submission of the counsel, a partner could claim deduction u/s 36(1)(iii) in his own assessment in respect of the interest paid on monies borrowed for investment on partnership and that a partner is, under the law, carrying on

business even though the business is actually run through the mechanism of a partnership. He contended also that the expenditure itself would amount to a loss allowable as such in the assessment.

8. For the department, the submission, in short, was that expenditure in relation to one firm could not be adjusted against the share of profit from the others, that the payment of interest was only an expenditure and should not be treated as loss and that Section 67(3) which was the only provision applicable to the facts here, did not justify the claim for allowance.

9. Before proceeding further, we would set out the relevant provisions which are material on the facts here. Section 36(1)(iii) in so far as it is relevant runs as follows :

36. (1) The deductions provided for in the following clauses shall be allowed in respect of the matters dealt with therein, in computing the income referred to in Section 28--.....

(iii) the amount of the interest paid in respect of capital borrowed for the purposes of the business or profession.

10. There is an Explanation to this provision in Sub-clause (iii) to which reference is not necessary.

11. Section 67(3) runs as follows :

67. (3) Any interest paid by a partner on capital borrowed by him for the purposes of investment in the firm shall, in computing his income chargeable under the head "profits and gains of business or profession" in respect of his share in the income of the firm, be deducted from the share.

12. As we are mainly concerned with Section 36(1)(iii) which is referred to in the question, we have to examine the contention in the light of that provision. The forerunner to this provision under the Act of 1922 was Section 10(2)(iii), which ran on identical terms. That provision had come in for consideration before this court and also other courts on a number of occasions. The earliest case on this point is that in *The Commissioner of Income Tax Vs. M.T.T.K.M.M.S.M.A.R. Somasundaram Chettiar*, . In that case the assessee carried on business at various places, including Madras where his head office was, and Ipoh, a place in the Federated Malay States. He borrowed money in Madras and paid interest thereon in

Madras. Part of that money was sent out to Ipoh and was used as capital in the conduct of the Ipoh business. Deduction was claimed in respect of

the interest paid by the assessee on his borrowings. The question before the court was whether the interest paid to the extent referable to the

remittances to Ipoh was liable to deduction in India. At that time the income from a foreign business was not liable to tax except when the profits

were remitted and that too within a period of three years of being earned. At page 487 this court observed :

The question is, can this capital be said to be borrowed "for the purposes of the business"? What is the business ? Obviously, the business whose

profits are being assessed to taxation.

13. The learned judges pointed out that to allow deductions in respect of interest on borrowed capital on the facts there would be inconsistent with

the whole tenor and language of the Act and in their view-

"the business" meant the business whose profits were being assessed in the year under consideration.

14. The same question came up for consideration before the Bombay High Court in *In Re: The Provident Investment Co. Ltd.*, . In that case the

Provident Investment Company Ltd., the assessee, an Indian finance company, borrowed some money in India and purchased Sterling securities

out of it and retained them in India. The Bombay High Court held that:

Now looking at that Section again in the light of the context, tax is to be payable by an assessee under the head of "Business" in respect of the

profits or gains of any business carried on by him. Clearly that must mean in respect of the taxable profits or gains of any business carried on by

him, and the business must be one which earns taxable profits or gains. Then, when we come to Sub-section (2)(iii) an allowance is to be made in

respect of interest on capital borrowed for the purposes of the business. Now, I think that again must be for the purposes of the business which

earns or is capable of earning taxable profits. Whether or not in fact taxable profits are earned is not necessarily the criterion, because the

borrowed money may earn no profit, but I think the " business " referred to in that Section is a business which is so carried on that taxable profits

may be earned, and unless it is a business of that character a deduction for interest on capital money borrowed for the purposes of that business is

not allowable under the Act.

15. These cases were cited before and distinguished on facts by the Supreme Court in Commissioner of Income Tax, Madras Vs. Indian Bank

Ltd., . The Supreme Court pointed out that in both The Commissioner of Income Tax Vs. M.T.T.K.M.M.S.M.A.R. Somasundaram Chettiar, and

In Re: The Provident Investment Co. Ltd., there was no single business but the businesses in India and abroad were distinct and separate. Under

both these decisions, the claim for deduction of interest had to be examined from the angle as to whether from the investment or outlay of the

borrowed monies, profits assessable to Income Tax can be earned so that an allowance can be claimed under the then Section 10(2)(iii). If no

such profits could be earned, then, the interest to that extent could not be allowed as deduction.

16. The question as to whether the interest is liable to be allowed as deduction in the case of a single business activity where part of the activity

resulted in non-taxable profits, has come up for consideration in other decisions. In S.A.S.S. CHELLAPPA CHETTIAR Vs. COMMISSIONER

OF INCOME TAX, MADRAS., the assessee was carrying on business as a money-lender who borrowed money and lent it out to constituents.

He was obliged, in the course of this business, to receive agricultural lands in repayment of his debts from such constituents. The question was

whether he was entitled to deduction of the interest paid by him on so much of the capital borrowed for business purposes as was represented by

the agricultural lands got in, u/s 10(2)(iii) of the Act of 1922, in computing the profits and gains of his money-lending business. When the matter

came on reference to this court, it quoted with approval the passage from the judgment in Provident Investment Company Ltd., In re set out

already. This court held, after discussing the other authorities on the point, that the agricultural activities of the assessee were inextricably mixed

with and incidental to the money-lending business and that the assessee was not to be deprived of the advantages conferred by Section 10(2)(iii)

because the capital benefiting therefrom happened to produce a non-taxable income.

17. The same question as to whether in a single business there could be a partial disallowance, came up before the Supreme Court in a few cases.

In Commissioner of Income Tax, Bombay Vs. C Parakh and Co. (India) Ltd., the assessee carried on a single business at a number of places. In that case the Supreme Court was concerned with the head office in Bombay and a branch office at Karachi. The assessee was carrying on large-scale business in cotton both in Bombay as well as in Karachi. It made a total profit of over Rs. 15,00,000, of which roughly Rs. 9,00,000 represented the profits earned in Bombay and Rs. 6,00,000 at Karachi. It had a managing agent to whom remuneration had been paid at the rate of 20 per cent. of the profits. The assessee debited the Bombay head office with Rs. 1.89 lakhs and the Karachi branch with Rs. 1.24 lakhs as managing agency remuneration. It, however, claimed, that the whole of Rs. 3.13 lakhs paid as managing agency remuneration was debitable to the Bombay office. It may be mentioned here that the profit at Karachi was subject to an abatement under the provisions of an agreement with Pakistan. The question that really arose before the Supreme Court was whether the assessee was eligible for the abatement on the whole of the profit earned in Karachi without any deduction of the managing agency remuneration debited in the accounts as relating to Karachi or the net figure after deducting the proportionate remuneration of the managing agency as debited to the Karachi office. The Supreme Court held that the assessee was eligible for the deduction of the whole of the commission of Rs. 3.13 lakhs in India and that the profit eligible for abatement under the agreement was the whole of the profit earned there without reference to the debit of proportionate managing agency remuneration as in the accounts. The Supreme Court arrived at the same result by pointing out that the agreement providing for the managing agency remuneration contemplated the deduction of the entire amount at the head office in Bombay. The relevancy of this decision, which is cited on behalf of the assessee before us, is to show that even where a part of the profits is not liable to tax in India, the expenditure incurred for earning the profits was not liable to be disallowed in India. As indicated earlier, in the case of a single business, there is no question of disallowance of a part of the expenditure merely because to the extent of a part of the income there was no liability to tax in India. This position emerges more clearly from the two later decisions of the Supreme Court.

18. In Commissioner of Income Tax, Madras Vs. Indian Bank Ltd., . the assessee, the Indian Bank, in the course of its business, invested a large

sum in Government securities, including securities the interest from which was exempt from tax. The question before the Supreme Court was

whether the interest paid by the bank on monies borrowed had to be allowed in its entirety u/s 10(2)(iii) of the Act of 1922 or could be disallowed

proportionately to the extent invested in tax-free securities. At page 80 Sikri J., as he then was, observed :

Sub-section(i) (to Section 10 of the Act of 1922) directs that an assessee be taxed in respect of the profits and gains of business carried on by

him. What is the business of the assessee must first be looked at. Does he carry on one business or two businesses or along with the business

carried on by him some activity which is not a business ? If he is carrying on an activity which is not business, we must leave out of account the

receipts of that activity. That is the first step. Secondly, we must look at Section 10(2) and deduct all the allowances permissible to him. In allowing

a deduction which is permissible the question arises : Do we look behind the expenditure and see whether it has the quality of directly or indirectly

producing taxable income ? The answer must be in the negative.....The legislature stops short at directing that it be ascertained what was the

purpose of the expenditure. If the answer is that it is for the purpose of the business, Parliament is not concerned to find out whether the

expenditure has produced or will produce taxable income.

19. At page 82, their Lordships stated that the business of the Indian Bank could not be divided into two separate businesses and that it was one

and indivisible. The principle laid down in this case had, therefore, to be construed in the light of this position of the existence of a single business.

20. In Commissioner of Income Tax, Bombay Vs. Maharashtra Sugar Mills Ltd., Bombay, . the facts were as follows: The assessee owned

extensive lands on which he grew sugar-cane and used the sugar-cane for the manufacture of sugar in its factory. The finding of the Tribunal was

that the cultivation of sugar-cane and the manufacture of sugar constituted one single and indivisible business. The question was whether a part of

the managing agency commission paid by the company could be disallowed on the ground that that part related to management of sugar-cane

cultivation, income from which was exempt from tax as agricultural income. The Supreme Court held that the entire managing agency commission

was laid out or expended for the purpose of the business carried on by the assessee. The fact that the income from a part of the business was not

exigible to tax under the Act was not, it was considered, a relevant circumstance.

21. Having regard to the decisions cited above and in particular the cases of the Commissioner of Income Tax, Madras Vs. Indian Bank Ltd., and

of the Maharashtra Sugar Mills, it is clear that the principle applicable to a case where an assessee carried on a single business part of whose

profits is not assessable to tax is different from a case where the assessee carries on more than one business. From the fact that the Supreme Court

has quoted with approval the decisions of the Madras High Court in The Commissioner of Income Tax Vs. M.T.T.K.M.M.S.M.A.R.

Somasundaram Chettiar, . and of the Bombay High Court in Provident Investment Company Ltd., In re, s; 6 ITC 21 (Bom). and from the

distinction made between the two types of cases in both the cases of the Commissioner of Income Tax, Madras Vs. Indian Bank Ltd., . and the

Commissioner of Income Tax, Bombay Vs. Maharashtra Sugar Mills Ltd., Bombay, . the principle applicable to these two sets of cases is clearly

different. It is thus necessary to keep the distinction between these two types of cases in considering the question of deductibility of the

expenditure. In the present case there is a finding by the Tribunal, which is binding on us, that the businesses carried on by the assessee through

three different firms do not constitute a single business. This finding as such was not attempted to be challenged. In these circumstances, we have to

apply the law as laid down consistently in cases where the assessee carries on distinct and separate businesses, and exclude from deduction the

interest in so far as it related to the non-taxable activity.

22. We have so far discussed the question as if it is bereft of authority binding on us. Mr. Jayaraman for the Commissioner of Income Tax brought

to our notice the decision in P. Rm. S. Ramanathan Chettiar Vs. Commissioner of Income Tax, which appears to us to conclude the issue before

us. In that case the assessee was doing money-lending business and was also receiving income as a partner in an agricultural estate. In computing

his income from the money-lending business, he claimed deduction of a sum of

Rs. 20,700 by way of interest on borrowed money. Out of this amount the Income Tax Officer disallowed a part being the portion of the interest referable to the capital of the assessee in one of the estates on the ground that the expenditure by way of interest was not to that extent laid out wholly and exclusively for the purpose of the assessee's business of money-lending. The disallowance was confirmed on further appeals before the Appellate Assistant Commissioner and the Tribunal. In that case, at page 537 this court, on reference, observed:

In fact it (section 10 of the Act of 1922) says that profits or gains will be computed after making allowance in respect of interest paid on the capital borrowed for the purpose of the business. That means, to our minds, that the borrowing, in order to come within the provision, should be for the purpose of a particular business...

23. After referring to the decision of the Supreme Court in Commissioner of Income Tax Vs. P.M. Muthuraman Chettiar and Another, . it was pointed out:

In passing we may also notice from the excerpt (from that decision set out in the same page) the indication that the profits of each distinct business may have to be computed separately and it is in such computation the application of one or other relevant provision u/s 10(2) may arise. For instance, if an assessee carries on more than one business, a textile business and a cloth shop, and he incurs expenditure in the former which results in a loss but in the other business profits are derived, it is obvious, as we are inclined to think, that the expenditure incurred in carrying on the textile business cannot properly be allowed as a deduction from the profits and gains derived from the cloth shop.

24. This court came to the conclusion that the assessee was not entitled to the deduction as claimed. But the matter was remanded to the Appellate Tribunal to find out whether the assessee's contention that there was no borrowal at all so as to justify the disallowance was correct or not.

Respectfully following this decision also, we have to hold that the assessee cannot claim deduction for the interest paid for the investment in the firm

owning agricultural lands out of the share income from the other two firms. The clear principle laid down in the above decision is that the

expenditure of one business cannot be permitted to be deducted from the

income from another business. The reason for this conclusion is obvious.

There are two stages in an assessment. The Income Tax Act has dealt with the income from different heads under different sets of provisions.

Where one considers, for instance, the head "Business", it is necessary to find out whether the assessee carried on a single business or more than

one business. If he carries on a single business, there is no difficulty in accepting the claim for deduction of a common item of expenditure, for, the

fact that a part of the profits of the single business was not liable to be taxed, had no relevance in the disposal of the case for deduction. If,

however, the assessee carried on more than one business, the claim for deduction in respect of each such business will have to be exempted. It is

only after this first stage of arriving at the final result of each such business that the respective amounts of income will have to be aggregated and

brought to tax under the head "Business". Thus, the stage of aggregation is posterior to the stage of examining the claim for deduction of any

particular item of expenditure. Where an assessee is left with some expenditure which he cannot get deducted in the absence of a taxable source,

then he cannot get the deduction from any other business to which it does not relate. Any business expenditure has to be related to a business

which is taxed or taxable, before it can be deducted. There is no scope for deduction of interest here, as there is no business income, taxed or

taxable, to which it relates.

25. We are not impressed with the argument of the learned counsel for the assessee that this decision in *P. Rm. S. Ramanathan Chettiar Vs.*

Commissioner of Income Tax, is in any manner inconsistent with the language of the earlier authorities on this point. We may briefly refer to those

authorities which, it was contended, took a different view. The *Commissioner of Income Tax Vs. A. Suppan Chettiar and Co.*, was a case

decided by this court. The assessee, an unregistered firm, claimed adjustment for depreciation on the machinery, plant, etc., used for the purpose

of the business against the profits and gains of other businesses. In that case the assessee, among others, carried on a business in plying motor

service. The income from this business, before adjustment of depreciation, was Rs. 253. The depreciation claimed on the buses exceeded Rs.

10,000. As it was not possible to adjust the said depreciation allowance against

the income of Rs. 253, from the buses, the claim of the assessee was that the unabsorbed depreciation should be adjusted against the income from other businesses. The claim urged on behalf of the Income Tax department was that under proviso (b) to Section 10(2)(vi) of the Act of 1922, the claim for unabsorbed depreciation had to be carried forward and added to the claim for depreciation in the following year. In other words, the contention was that the loss which resulted from the non-adjustment of the entire depreciation claimed had only to be carried forward and could not be adjusted against the other business income of the relevant year. This court observed :

We do not think therefore that upon the terms of the Section an assessee is precluded from adding the whole charge for depreciation to his other business charges, even though the result is to show a loss, and then claiming u/s 24 to set off the loss against profit from other sources. Nor have we been shown that there is anything in the nature of this allowance for depreciation to render such a course inadmissible.

26. The same question arose for the consideration of the East Punjab High Court in LAXMICHAND JAIPORIA SPINNING AND WEAVING MILLS, IN RE., and the conclusion was identical.

27. In Ambika Silk Mills Co. Ltd. Vs. Commissioner of Income Tax, Bombay City, the question of the adjustability of unabsorbed depreciation against capital gains arose. The assessee had derived capital gains to the extent of Rs. 90,400. The business income of that year came to Rs.

37,703. The depreciation claimed was Rs. 52,985. There was thus a balance of unabsorbed depreciation of Rs. 15,282. The assessee contended

that this unabsorbed depreciation had only to be carried forward and could not be set off against Rs. 90,400 determined as capital gains. The

reason for this plea of the assessee was that the sum of Rs. 90,400 was eligible for relief from super-tax. The Income Tax authorities did not

dispute the eligibility of the claim of the assessee for his relief in respect of the capital gains. They, however, took the view that the capital gains had

to be reduced to Rs. 15,282 so that the assessee would be eligible for the relief from supertax only to the extent of the balance. It is in

consideration of this claim that the Bombay High Court examined the question of adjustment of an unabsorbed depreciation. While pointing out

that the unabsorbed depreciation could be adjusted against the capital gains, the court held that the assessee was eligible for relief on the entire sum

of Rs. 90,400 earned as capital gains. This was on a construction of the provisions of Section 17(7) of the Income Tax Act of 1922.

28. These decisions do not, in our opinion, run counter to the decision of this court in *P. RM. S. Ramanathan Chettiar v. Commissioner of Income*

Tax [1969] 74 ITR 534 . In each of these cases, when examined, it would be found that there was a computation of the loss as a result of the non-

adjustment of the unabsorbed depreciation. The matter arose at the stage of aggregation representing the second stage. When once the result has

been arrived at (first stage) and unfortunately the result showed a loss, then that would not in any way preclude the adjustment of the loss. But that

is not the position here.

29. Two other decisions on which strong reliance was placed on behalf of the assessee as if they point to a different result, may now be noticed.

The first one is reported in *Mohamed Ghouse Vs. Commissioner of Income Tax, Madras*, . In that case, the assessee was the owner of a transport

business. He borrowed monies for purchasing shares in another transport company and claimed the interest paid on the money borrowed as

deduction u/s 10(2)(iii) or alternatively u/s 12(2) of the Act of 1922. The shares which had been purchased with the aid of the borrowed money

had not yielded any dividend in the relevant year. This court examined the question of allowability of the interest in relation to Section 10(2)(iii) and

negatived it. The deduction was, however, allowed u/s 12(2) and it was pointed out that to allow a claim for expenses u/s 12(2) of the Act of

1922, it was not necessary that there should be income assessable to tax under the head ""Income from other sources"" referred to in Section 12(1)

of that Act. If there was no such income, the expenses would amount to a loss which would be available to the assessee to be adjusted against

other heads of income u/s 24(1) of the Act. The learned counsel for the assessee pressed into service the observation at page 135 that:

If there is no such income (assessable to tax) the expenses would amount to a loss which will be available to the assessee to be adjusted against

the other heads of income u/s 24(1) in the same year.

30. The fact that this court was considering the claim u/s 12(2) after negating

the claim u/s 10(2)(iii) cannot be lost sight of. Further, the income which was liable to be earned from the shares as dividends could be brought to tax u/s 12, when earned. If the purpose of the assessee to earn the income by making the investment failed, it was considered to be a common misfortune to the revenue as well as the assessee. An expenditure remaining unadjusted will have the quality of loss only after computation under the Act. There is no scope for any such computation here, as far as Riverdale Estate is concerned. Further, loss cannot be the subject of consideration u/s 36(1)(iii). The learned counsel for the assessee pointed out that in a later year the interest income and income from the sale of trees had been brought to tax. But those facts have not been adverted to in the statement of the case and are outside our purview. We cannot, at this stage, go into fresh facts adverted to by the assessee.

31. The learned counsel for the assessee sought the aid from another principle, viz., that business carried on by a firm was the business carried on by the partners and the profits of the firm were the profits earned by all the partners. This principle has been laid down by the Supreme Court in Commissioner of Income Tax, Bihar Vs. Ramniklal Kothari, . In that case the assessee, who was a partner in four firms, incurred expenditure by way of payment of salary and bonus to staff, expenses for maintenance and depreciation of motor car, travelling expenses and interest against the share of income from the firms. The claim came to be considered in the light of the provisions of the Act of 1922. At that time, it may be mentioned here that there was no provision parallel to Section 67(3) of the Act of 1961, which has already been extracted earlier in this judgment. The Supreme Court observed at page 59 :

Business carried on by a firm is business carried on by the partners. Profits of the firm are profits earned by all the partners in carrying on the business. In the individual assessment of the partner, his share from the firm's business is liable to be taken into account u/s 10(1). Being income from business, allowances appropriate u/s 10(2) are admissible before the taxable income is determined.

32. At page 60 it was pointed out that Section 23(5)(a)(ii) or Section 16(1)(b) of the Act of 1922 did not stand in the way of the allowance of these deductions and it was pointed out:

The receipt by the partner is business income for the purpose of Section 10(1), and being business income, expenditure necessary for the purpose

of earning that income and appropriate allowances are deductible therefrom in determining the taxable income of the partner.

33. We are not in this case considering the question as to whether the assessee is eligible for any further deduction for expenditure incurred by him

as a partner in order to earn the share income from a partnership, i.e., Riverdale Estate, producing taxable income, to apply this principle. The

propositions laid down this decision cannot be taken in the abstract, so as to rub out all distinctions between all businesses of an assessee and

require allowance of expenditure of one against the income from another. Another decision cited by the counsel for the assessee which remains to

be noticed is that of the Kerala High Court in *N. Sundareswaran Vs. Commissioner of Income Tax*, . The assessee was conducting a tin factory.

He formed a partnership with his wife and minor children for setting up a tin printing factory. It had not commenced production in the relevant year.

He advanced a sum of Rs. 1,68,334 to this firm for running the business of tin printing factory. He claimed allowance for interest on the said

amount. The Kerala High Court upheld the claim of the assessee u/s 10(2)(iii) of the Act of 1922. What is to be borne in mind in examining this

decision is that the assessee in that case was liable to be taxed on the share income from the said firm. It was not a case where the activity was

outside the scope of the Income Tax Act. The principle applicable to such a case is different from the principle applicable to a case where the

income is outside the purview of the Income Tax Act itself. In fact, agricultural income is not something which is otherwise assessable to tax under

the Income Tax Act but which was exempted from payment of such a tax. Agricultural income is so wholly outside the scope of the legislative

power that the exemption thereof set out in Section 10(1) of the Income Tax Act, 1961, can only be taken to be a clarificatory provision. Even

without the exemption conferred by Section 10(1), agricultural income would not be liable to tax. Therefore, it is not possible to take the view that

but for the exemption, the income would be liable to tax as happened in the case of tax-free securities dealt with in the decision of the

Commissioner of Income Tax, Madras Vs. Indian Bank Ltd., .

34. One other decision cited by the counsel is the one reported in R.M. Chidambaram Pillai and Another Vs. Commissioner of Income Tax,

Madras, . In that case the assessee received salary from a partnership which owned a tea estate. The question was whether the entire salary

income was liable to be taxed or only 40 per cent. thereof was liable to tax, in accordance with the provisions of Rule 24 of the Income Tax Rules,

1922. This court held that the salary received by a partner is only a share of profits allocated to him by the firm. The consequence was that only 40

per cent. of the salary was liable to be taxed under the Indian Income Tax Act, 1922. We are not concerned, in the present case, with any receipt

by a partner from a firm earning agricultural income in whole or in part, being treated as agricultural income. What applies to receipt is not always

applicable to a payment. The conclusion that the receipt of salary was receipt of a share of income was based on the particular provisions of the

Act. Those provisions do not, in any manner, apply to what is paid by a partner to a firm. We, therefore, do not find anything in R. M.

Chidambaram Pillai v. Commissioner of Income Tax to assist the assessee in the present case.

35. For the reasons mentioned above, the assessee is not eligible for the deduction u/s 36(1)(iii) of the Act, because the interest has been paid on

amounts invested on agricultural lands which are outside the scope and purview of the Income Tax Act, 1961. Further, as pointed out by the

learned counsel for the Commissioner, Section 67(3) would appear to negative the assessee's claim. Section 67 deals with the method of

computing a partner's share in the income of the firm. Sub-clause (3) thereof provided for the deduction of interest paid on capital borrowed for

the purpose of investment in the firm. As a specific provision has been made u/s 67(3) with reference to the claim for deduction of interest from the

share of income, it would follow that Section 36(1)(iii), which is in the nature of a general provision relating to all businesses, would have no

application. Section 67(3) provides for the deduction of any interest paid by the partner on capital borrowed by him for the purpose of investment

in the firm. It proceeds on the basis that in computing the income chargeable on the profits and gains of business or profession, which the share

income would come under, interest paid could be deducted from the share. There must be some share income in order to justify the assessee's

claim for deduction u/s 67(3). When there is none, it is not possible to accept the claim for deduction under that provision. When the claim for

deduction under this provision is negated, it is not possible to fall back u/s 36(1)(iii) for a consideration of the same claim as, as pointed out

already, in the case of interest payable by a partner for investment in a firm, the claim has to be considered only u/s 67(3) and not under any other

provision. In this view also, the claim u/s 36(1)(iii) has to be negated.

36. Though the question mentions whether any "part" of the claim of the assessee could be allowed as deduction, there was no point taken before

us that the figures required any further adjustment for any reason whatsoever. With reference to the amounts set out in the question, the answer is

that the disallowance is lawful. In other words, the question is answered in the affirmative and against the assessee in the respective cases.

37. Commissioner will be entitled to his costs which we fix at Rs. 250.