

(1991) 04 GAU CK 0010

In the Gauhati High Court

Case No : Income-tax Reference No. 19 of 1976 (Gauhati) and Income Tax Reference No. 1 of 1977 (Imphal Bench)

Commissioner of Income Tax

APPELLANT

Vs

Hardware Exchange

RESPONDENT

Date of Decision : 03-04-1991

Acts Referred:

Income Tax Act, 1961 — Section 40A(1), 40A(3)
Income Tax Rules, 1962 — Rule 6DD

Citation : (1991) 95 CTR 183 : (1991) 190 ITR 61

Hon'ble Judges : H.K. Sema, J;B.P. Saraf, J

Bench : Division Bench

Advocate : Y. Imo Singh, for the Appellant; L. Nandakumar Singh, for the Respondent

Judgement

This Judgment has been overruled by : M/s. Attar Singh Gurmukh Singh, etc. Vs. Income Tax Officer, Ludhiana, etc., (1991) 3 CompLJ 58(1)

B.P. Saraf, J.—By this reference u/s 256(1) of the Income Tax Act, 1961, made at the instance of the Commissioner of Income Tax, North Eastern Region, Shillong (Commissioner of income tax), the Income Tax Appellate Tribunal Gauhati Bench, Gauhati, has referred the following question of law to this court for opinion ;

"Whether, on the facts and in the circumstances of the case, the payments made for the purchase of stock-in-trade amount to expenditure within the meaning of Section 40A(3) of the Income Tax Act, 1961, read with Rule 6DD of the Income Tax Rules, 1962 ?"

2. The facts of the case are as follows. The assessee is a registered firm carrying on business in hardware. For the assessment year 1970-71 (corresponding to the previous year Ram Navmi 2026), the assessee-firm submitted its return of income showing the taxable income from business at Rs. 7,860. A copy of the profit and loss account was also filed. In the course of examination of the books

of account for the purposes of assessment, the Income Tax Officer noticed that the assessee had purchased corrugated aluminium sheets and hardware to the tune of Rs. 1,94,229 during the relevant previous year from a firm named M/s. Jamunalal Mangilal and Co. It was found that on 12 occasions during the year, the assessee paid sums exceeding Rs. 2,500 on account of purchase of goods to the said firm in cash and not by crossed cheque or crossed bank draft. The total of such payments came to Rs. 98,100 out of which a sum of Rs. 10,500 had been paid before March 31, 1969. The amounts so paid in-cash on or after April 1, 1969 amounted to Rs. 83,100. The Income Tax Officer issued a notice to the assessee to show cause as to why the aforesaid amount of Rs. 83,100 should not be added back to its income under the provisions of Section 40A(3) of the Act. The assessee in its reply claimed that the payments made were genuine and were made in cash for mutual convenience. The Income Tax Officer found that the wives of two of the partners of the assessee-firm were partners of the firm, M/s. Jamunalal Mangilal Land Co. from whom the purchases in question were made. On a consideration of the facts and circumstances of the case, the Income Tax Officer came to the conclusion that the payments in question made by the assessee to the said firm were genuine. He was, however, of the opinion that the proof of identity of the payee and/or genuineness of the payment was not enough to satisfy the requirement of Section 40A(3) of the Act. He was not satisfied with the explanation given by the assessee for not making the payments by crossed cheque or crossed bank draft. He, therefore, held that the said payment infringed the provisions of Section 40A(3) of the Act. Accordingly, a sum of Rs. 83,100 was added back to the total income of the assessee. On appeal, the Appellate Assistant Commissioner of Income Tax held that the payments in question having been made in respect of liabilities created by regular purchase of trade articles did not amount to expenditure deductible from the net profit. In that view of the matter, he held that the payment of Rs. 83,100, on account of purchase of trade articles, made by the assessee was not an expenditure and, as such, the provisions of Section 40A(3) were not attracted. In that view of the matter, the addition made by the Income Tax Officer was deleted.

3. The Revenue appealed to the Income Tax Appellate Tribunal. The Tribunal upheld the finding of the Appellate Assistant Commissioner. Following its earlier order, the Tribunal held that sums paid for the purchase of goods for business cannot be said to be expenditure within the meaning of Section 40A(3) of the Act. The Tribunal, therefore, confirmed the order of the Appellate Assistant Commissioner and dismissed the appeal of the Revenue. Aggrieved by the order of the Tribunal, the Commissioner of Income Tax filed an application for referring certain questions of law relating to the interpretation of Section 40A(3) of the Act to the High Court. Accordingly, the aforesaid question was referred.

4. The determination of the controversy in this case, therefore, revolves round the construction of Section 40A(3) of the Act and Rule 6DD of the Income Tax Rules. The question for determination is whether payments made for purchase of

trade articles or goods for sale, commonly known as "stock-in-trade" can be construed as payments in respect of any expenditure. It will be necessary for this purpose to find out the true meaning of the words "Payments in respect of any expenditure" to determine whether "expenditure" can be so widely interpreted to include payments on account of purchase of stock-in-trade. Another aspect that arises for consideration is whether payments exceeding Rs. 2,500 in respect of expenditure incurred made in cash for facility of suppliers or vendors can be disallowed u/s 40A(3) of the Act even in a case where the transactions are held to be genuine. This aspect, however, is no more *res Integra*. It was elaborately discussed by a Division Bench of this court in *Paul Brothers Vs. Commissioner of Income Tax*, where the Chief Justice, A. Raghuvir, speaking for the Bench, on a consideration of the various decisions of different High Courts on the subject, held that where the assessee tendered evidence that cash payments were made for facility of suppliers or vendors, the Tribunal was not justified in rejecting the explanation. It was observed (p. 359) :

"In the instant case, the five firms to whom payments were made, were all based at Gauhati. The assessee-firm is at Tezpur. Normally, the transactions are made "through accounts". But, in the above five instances, the representatives of the Gauhati firms "came to Tezpur" and "insisted" on cash payment (as in the Calcutta case). The assessee, therefore, had to pay in cash. This explanation was accepted by the Commissioner of Income Tax (Appeals) but not by the Income Tax Officer and the Tribunal. None of the three authorities have doubted the genuineness of these payments. Once the transactions are genuine, what is to be considered is only the explanation offered by the assessee.

We may now refer to the unconscionable delays that occur in the banking system of the country as often it is seen that cheques do not bring forth cash for months, sometimes the delay is of three or four months. That explains why cheques and drafts are not popular with the Indian businessmen. In the instant case, the assessee tendered evidence that the representatives of the five firms at Tezpur insisted on cash payments and, for the facility of the suppliers or vendors, the assessee paid in cash. The Tribunal, therefore, was not justified in rejecting the explanation..."

5. In the aforesaid case, a contention was also raised by the assessee that payments made for goods purchased were not to be construed as "expenditure". The court did not examine this contention as it was not necessary to do so in that case in view of the aforesaid finding. This point was, therefore, left open. It was observed :

"A word may be stated here. One of the arguments advanced before us on behalf of the assessee was that payments made for goods purchased are not to be construed as expenditure. On this question, we keep the matter open to be decided in a more appropriate case."

6. In the instant case also, the finding of all the authorities including the Income

Tax Officer himself is that the payment to the tune of Rs. 83,100 made by the assessee to M/s. Jamunalal Mangilal and Co. for supply of goods was genuine. The amount was added back to the income of the assessee as the Income Tax Officer was not satisfied with the explanation of the assessee in regard to payments made in cash and not by crossed cheque or crossed bank draft. So far as applicability of Section 40A(3) to payments on account of purchases is concerned, evidently the Income Tax Officer was of the opinion that such payments amounted to "expenditure" and Section 40A(3) was attracted. Both the appellate authorities--the Appellate Assistant Commissioner as well as the Tribunal--did not approve the interpretation of the Income Tax Officer and held that payments made for purchase of trade articles or stock-in-trade do not amount to expenditure inasmuch as no deduction is claimed by an assessee in the computation of his taxable income on account of such payments. It was, therefore, held that Section 40A(3) had no application to such payments. The addition of Rs. 83,100 made by the Income Tax Officer to the income of the assessee was, accordingly, held to be not tenable. In view of the aforesaid conclusion, the appellate authorities did not consider the claim on the other aspect whether, in view of the finding of the Income Tax Officer that the payments were genuine, the amount could have been added to the income of the assessee or not. Under the circumstances, the only question of law that has been referred to us for decision is whether on a proper interpretation of Section 40A(3) of the Act, payments made for purchases of goods are to be construed as expenditure. Section 40A, so far as relevant, reads :--

"40A. Expenses or payments not deductible in certain circumstances.--(1) The provisions of this section shall have effect notwithstanding anything to the contrary contained in any other provision of this Act relating to the computation of income under the head "Profits and gains of business or profession"...

(3) Where the assessee incurs any expenditure in respect of which payment is made, after such date (not being later than the 31st day of March, 1969) as may be specified in this behalf by the Central Government by notification in the Official Gazette, in a sum exceeding two thousand five hundred rupees otherwise than by a crossed cheque drawn on a bank or by a crossed bank draft, such expenditure shall not be allowed as a deduction :...

Provided further that no disallowance under this sub-section shall be made where any payment in a sum exceeding two thousand five hundred rupees is made otherwise than by a crossed cheque drawn on a bank or by a crossed bank draft, in such cases and under such circumstances as may be prescribed, having regard to the nature and extent of banking facilities available, consideration of business expediency and other relevant factors."

7. Sub-section (3) was amended by the Direct Tax Laws (Amendment) Act, 1987, and, the words "two thousand five hundred rupees" were substituted by "ten thousand rupees" with effect from April 1, 1989.

8. From a bare reading of the aforesaid provision, it is clear that it has an overriding effect over all other provisions of the Act. Sub-section (1) declares in express terms that an expenditure or allowance which is otherwise deductible under any provision of the Income Tax Act relating to the head "Business or profession" may be disallowed under this section. Sub-section (3) deals with "expenditure incurred" by an assessee and provides for disallowance of such expenditure as a deduction if the payment in respect thereof in a sum exceeding the specified limit (Rs. 2,500 at the relevant time) is made otherwise than by a crossed cheque or a crossed bank draft unless the case falls within any of the exceptions as may be prescribed having regard to the nature and extent of the banking facilities available, consideration of business expediency and other relevant factors.

9. The exceptions have been prescribed in Rule 6DD of the Income Tax Rules, 1962. The rule so far as relevant reads as follows :

"6DD. Cases and circumstances in which payment in a sum exceeding ten thousand rupees may be made otherwise than by a crossed cheque drawn on a bank or by a crossed bank draft,--No disallowance under Sub-section (3) of Section 40A shall be made where any payment in a sum exceeding ten thousand rupees is made otherwise than by a crossed cheque drawn on a bank or by a crossed bank draft in the cases and circumstances specified hereunder, namely :

(a) where the payment is made to--...

(b) where the payment is made to Government and, under the rules framed by it, such payment is required to be made in legal tender ;...

(f) where the payment is made for the purchase of-

(i) agricultural or forest produce ; or

(ii) the produce of animal husbandry (including hides and skins) or dairy or poultry farming ; or

(iii) fish or fish products ; or

(iv) the products of horticulture or apiculture to the cultivator, grower or producer of such articles, produce or products ;

(g) where the payment is made for the purchase of the products manufactured or processed without the aid of power in a cottage industry, to the producer of such products ;

(h) where the payment is made in a village or town, which on the date of such payment is not served by any bank, to any person who ordinarily resides, or is carrying on any business, profession or vocation, in any such village or town ;

(i) where any payment by way of gratuity, retrenchment compensation or similar terminal benefit is made to an employee of the assessee or the heirs of any such employee on or in connection with the retrenchment, resignation, discharge or

death of such employee, if the income chargeable under the head "Salaries" of the employee in respect of the financial year in which such retirement, resignation, discharge or death took place or the immediately preceding financial year did not exceed Rs. 7,500 ;

(j) in any other case, where the assessee satisfies the Assessing Officer that the payment could not be made by a crossed cheque drawn on a bank or by a crossed bank draft--

(1) due to exceptional or unavoidable circumstances, or

(2) because payment in the manner aforesaid was not practicable, or would have caused genuine difficulty to the payee, having regard to the nature of the transaction and the necessity for expeditious settlement thereof, and also furnishes evidence to the satisfaction of the Assessing Officer as to the genuineness of the payment and the identity of the payee."

10. In Clauses (a) to (i) of the aforesaid rule, certain payments have been specified which shall not fall within the sweep of Section 40A(3). Clause (j) is a residuary clause and, under this clause, as originally framed, the assessee might prove that the payment exceeding the specified limit could not be made by a crossed cheque or a crossed bank draft due to (1) exceptional circumstances or unavoidable circumstances. If that is done, Section 40A(3) shall not apply to such payments. This clause was amended with effect from April 1, 1970, and two more mitigating circumstances were added, namely, such payment was not practicable having regard to the nature of the transaction and the necessity for expeditious settlement thereof, or such payment would have caused genuine difficulty to the payee having regard to the nature of the transaction and the necessity for expeditious settlement thereof. Thus, under the amended Clause (j), proof as to the existence of any of the four circumstances enumerated in the two sub-clauses thereof will take the case out of the sweep of Section 40A(3) of the Act. However, even in such cases, the assessee is required to furnish satisfactory evidence as to the genuineness of the payment and the identity of the payee.

11. A number of clarifications and circulars were issued from time to time by the Central Board of Direct Taxes elaborating the scope and effect of Section 40A(3). By a letter dated April 10, 1969, issued by the Under Secretary, Central Board of Direct Taxes, it was made clear that payments made in advancing loans and returning the principal amount of borrowed moneys are not covered by the provisions of Section 40A(3) of the Act as these do not constitute "expenditure". However, by another letter dated April 18, 1969, issued by the Under Secretary, Central Board of Direct Taxes, addressed to a firm of tax practitioners, it was clarified that the word "expenditure" in Section 40A(3) covers expenditure of all categories "including that on purchase of goods and merchandise" as also payment for services. In fact, it is this interpretation of Section 40A(3) which appears to have led the officers of the Department to hold that payments on

account of purchase of goods are also to be construed as expenditure.

12. In the backdrop of the aforesaid provisions of Section 40A(3), Rule 6DD and the circulars of the Board, it is to be decided whether the provisions of Section 40A(3) would apply to payments made in respect of purchase of stock-in-trade or not. Evidently, the provisions of Sub-section (3) are applicable only to a case where the assessee "incurs any expenditure" in respect of which any payment is made. The real question for determination, therefore, is whether payments made on account of purchase of goods, merchandise or stock-in-trade can be construed as payments made in respect of any "expenditure incurred" by the assessee.

13. This question came up for consideration before a number of High Courts. The earliest decision appears to be a decision of the Orissa High Court in *Sajowanlal Jaiswal Vs. Commissioner of Income Tax*, In this case, it was held that the expenditure referred to in Section 40A(3) is not confined to expenditure that could be claimed as deduction u/s 37 and refers to any payment made by the assessee and taken into account in computing the total income under the provisions of the Act, While arriving at the aforesaid conclusion, the High Court considered the fact that the expression "expenditure" has not been defined in the Act and observed that, in the absence of such a definition, all outgoings could broadly come under the head "expenditure". The court also referred to the provisions of Rule 6DD and observed that the said provisions throw considerable light on what exactly is the scope of Sub-section (3). It was, therefore, held that, in Sub-section (3), the word "expenditure" has been used in the widest amplitude and payment for purchase of goods would be an expenditure.

14. Next in order is the decision of the Allahabad High Court in *U.P. Hardware Store Vs. Commissioner of Income Tax*, In this case also, it was held that the word "expenditure" used in Sub-section (3) of Section 40A(3) was not restricted to overhead expenses enumerated in Sections 30 to 43A but it covered the expenses to be taken into account while determining the gross profit. It was, therefore, held that "payments made for purchases" would also be covered by the word "expenditure". It was observed (p. 667) :

"In enacting Section 40A(3), the intention of Parliament clearly was to prevent use of unaccounted money in carrying on business. Unaccounted money may be used in the purchase of stock-in-trade or raw materials or in payment of overhead expenses. We will be defeating the intention of the Legislature if we restrict the import of the word "expenditure" to merely overhead expenses and do not take into account the expenditure incurred on the purchase of stock-in-trade or raw materials."

15. In this case also, the provisions of Rule 6DD, particularly Clauses (f) and (g) which provide that an assessee can be exempted from the requirement of payments by crossed cheque or crossed bank draft in certain circumstances, were also referred to in support of the wider interpretation given to the expression "expenditure".

16. This decision and the decision of the Orissa High Court in *Sajowanlal Jaiswal Vs. Commissioner of Income Tax*, were followed by the Allahabad High Court in *Ratan Udyog Vs. Income Tax Officer and Another*, . It was held that, having regard to the wider meaning of the word "expenditure" so as to embrace whatever is paid out or away, there is no reason why payments made for the purchase of stock-in-trade or raw materials should not be regarded as expenditure for the purposes of Section 40A(3) of the Act.

17. The decision in *U.P. Hardware Store Vs. Commissioner of Income Tax*, was followed by the Allahabad High Court in all subsequent cases including *Addl. Commissioner of Income Tax Vs. Nathimal Badri Prasad and Another*, *Addl. Commissioner of Income Tax Vs. Ram Narain Kishan Gopal*, *Ideal Tannery Vs. Commissioner of Income Tax*, *Addl. Commissioner of Income Tax Vs. Radhey Shyam Jagdish Prasad*, *Commissioner of Income Tax Vs. Ganesh Trading Co.*, and *Addl. Commissioner of Income Tax Vs. Jamuna Dass Nemi Chand*,

18. The Kerala High Court also took the same view in *P.R. Textiles Vs. Commissioner of Income Tax*,

19. The Punjab and Haryana High Court fell in line with the High Courts of Orissa and Allahabad and in *Commissioner of Income Tax Vs. New Light Tin Manufacturing Company*, held that payments made for the purchase of goods fall within the meaning of the expression "expenditure" occurring in Section 40A(3). This decision was followed in *Commissioner of Income Tax Vs. Kishan Chand Maheshwari Dass*,

20. The Rajasthan High Court also considered this aspect of the matter in *Kanti Lal Purshottam and Co. Vs. Commissioner of Income Tax*, The court referred to the provisions of Clauses (f) and (j) of Rule 6DD which provide that payments for purchase of agricultural produce made in cash in certain circumstances shall not attract Section 40A(3) as an aid to the interpretation of the said section. However, in this case, the court did not decide the question of applicability of Section 40A(3) of the Act in view of its finding that the transaction was genuine and the identity of the payee was not in dispute. It was held that the genuineness of payment having been established, the default, even if made, was only technical and the assessee was entitled to exemption under Clauses (f) and (j) of Rule 6DD in respect of payments regarding such purchases.

21. However, Section 40A(3) was later interpreted by the Rajasthan High Court in *Fakri Automobiles Vs. Commissioner of Income Tax*, The court referred to the decisions of the Orissa, Allahabad, Kerala and Punjab and Haryana High Courts and following the same, held that the word "expenditure" in Section 40A(3) of the Act has wide import and it includes the price paid for the purchase of stock-in-trade and/or raw materials and such payments fall within the sweep of the said section.

22. In a later decision in *Kejriwal Iron Stores Vs. Commissioner of Income Tax*, the Rajasthan High Court again considered the meaning of the word

"expenditure" in Section 40A(3) to find out whether it includes payments made on account of purchase of goods and, following the decisions of the various High Courts referred to above, reiterated that such payments were covered by the word "expenditure".

23. This decision (sic) was followed in *Nahgi Lal Vs. Commissioner of Income Tax*, and in *Badrilal Phool Chand Rodawat v. CIT* [1987] 167 ITR 404.

24. The Patna High Court considered this question in *Commissioner of Income Tax Vs. Ram Chand Gobind Prasad*, and, following the decisions of the Orissa, Allahabad and Punjab and Haryana High Courts, held that expenditure as contemplated in Section 40A(3) of the Act includes expenditure on purchases relating to the trading account.

25. In *Venkatasatyanarayana Timber Depot Vs. Commissioner of Income Tax*, this question arose also before the Andhra Pradesh High Court. In this case also, the contention as to the applicability of Section 40A(3) to payments made for purchase of stock-in-trade was raised by the assessee. The court, however, did not consider it necessary to consider this contention in view of its findings that, under the facts and circumstances of the case, the assessee was entitled to avail of the exemption provided, under Rule 6DD.

26. We have given our careful consideration to the aforesaid decisions of the High Courts of Orissa, Allahabad, Kerala, Punjab and Haryana, Rajasthan and Patna wherein it has been held that payments made for purchase of stock-in-trade or raw materials should also be regarded as expenditure for the purpose of Section 40A(3) of the Act. The reasoning given in these decisions for arriving at the aforesaid conclusion may broadly be summed up as follows :

(1) In the absence of a statutory definition, the word "expenditure" should be given a wide interpretation so as to include payments made for purchase of stock-in-trade or raw materials :

(2) Such a wide interpretation should be made, in view of the fact that the intention of Parliament while enacting Section 40A(3) was to prevent use of unaccounted money in carrying on business and such a purpose will be frustrated if the import of the word "expenditure" is restricted to overhead expenditure and if it is held that it does not include expenditure incurred on purchase of stock-in-trade or raw materials ; and "

(3) Rule 6DD, more particularly Clauses (f) and (g) which lay down the exceptional circumstances under which payments for agricultural produce made in cash might not be disallowed, throw considerable light on the scope and ambit of Section 40A(3) and can be used as an aid to interpretation of the said section.

27. We have considered these reasonings or propositions as well as the decisions based thereon. We, however, find it difficult to agree with the same. In our opinion, for the purpose of proper determination of the controversy before us, it is necessary to ascertain the true meaning of the expression "expenditure

incurred" because it is only payments made in respect of expenditure incurred which are covered by Section 40A(3) of the Act--not all payments made by an assessee. This aspect appears to have been totally lost sight of in all the judgments referred to above. Emphasis has been laid on the words "payments made" than on "expenditure incurred" which, in our opinion, is not correct.

28. Payments are made by an assessee in the course of his business, on various accounts, e.g., for purchase of assets, including current assets or floating assets, advance of loans, expenditure, etc. All payments ipso facto cannot be termed as "expenditure" nor can all such payments be claimed as deduction in the computation of profits or income. In fact, no question of allowance or disallowance of all such payments as deduction does arise except in case of payments in respect of expenditure allowable under the Act. Payments for acquisition of assets are, in fact, investment--not expenditure. Section 40A(3) is confined to disallowance of "expenditure" in respect of which payment is made in cash beyond the specified limit--not all payments on whatever account. The two expressions "payment made" and "expenditure incurred" are not interchangeable. Payments may be made on various accounts--"expenditure incurred" is only one of them. Evidently, application of Section 40A(3) is confined to payments made in respect of "expenditure incurred". It does not extend to other payments. In that view of the matter, to determine whether payments made for purchase of stock-in-trade can be said to be payments in respect of "expenditure incurred", it is necessary to ascertain the true meaning of the expressions "expenditure" and "stock-in-trade".

29. The word "expenditure" has been defined in various dictionaries. In Random House Dictionary of the English Language, it has been defined to mean :

"1. The act of expending ; disbursement ; consumption.

2. that which is expended ..."

30. In Corpus Juris Secundum (Vol. 35), "expenditure" has been defined as follows :

"In its broader sense the word "expenditure" is any laying out or disbursement of money ; and the term is defined as meaning the act of expending ; disbursement, expense, money expended, a laying out, as of money, or the spending of money. The term does, however, often connote the using up or consumption of property. The meaning of the word is particularly governed by its context."

31. Similar are the definitions in various other dictionaries, but we do not propose to refer to all those in view of the decision of the Supreme Court in the context of the Income Tax Act itself in *Indian Molasses Co. (Private) Ltd. Vs. Commissioner of Income Tax, West Bengal*, where expenditure has been defined as follows (p. 78) :

""spending" in the sense of "paying out or away" money is the primary

meaning . . . "expenditure" is thus what is "paid out or away" and is something which is gone irretrievably".

32. Though this definition has been noticed by the High Courts in some of the decisions referred to above, it appears that while reading this definition, emphasis was laid only on the words "paid out or away" which resulted in the conclusion that whatever is paid out is expenditure. The courts lost sight of the fact that the Supreme Court, while defining expenditure as what is "paid out or away", had also added the expression "and is something which is gone irretrievably". The definition of expenditure as given by the Supreme Court was thus not read as a whole which resulted in its incorrect interpretation.

33. "Expenditure", generally speaking, means "spending--paying out of money". But that is too broad a definition and, read out of context, might lead to misleading interpretation. That is why the Supreme Court in *Indian Molasses Co. (Private) Ltd. Vs. Commissioner of Income Tax, West Bengal*, added to the definition of expenditure, the expression "and is something which is gone irretrievably". Every payment is not expenditure. Payment may be for acquisition of assets. Assets may be fixed assets or floating or circulating assets. Fixed, assets are assets of business which are of permanent nature and are held for the purpose of earning revenue and not with a view to resell, e.g., plant and machinery, buildings. Floating or current assets are those assets which are made or acquired and merely held for a short period of time, also with a view to sell at a profit in the ordinary course of business. These assets are easily convertible into cash and include stock, debtors, bills receivable.

34. The point that crops up for consideration, therefore, is--when stock-in-trade is acquired and money is paid for that purpose, whether the money so paid goes irretrievably. Evidently, that is not so. By such payment, goods are acquired which are termed as floating or current assets and the money so paid is likely to be recovered by sale of such assets in the course of business.

35. The expressions "stock" or "stock-in-trade" have been defined in various dictionaries, general as well as legal.

36. The Random House Dictionary of the English language defines stock-in-trade as :

"1. the requisites for carrying on a business, esp. goods kept on hand for sale in a store ..."

37. In *Oxford Advanced Learner's Dictionary of Current English* by A. S. Hornby, "stock" has been defined as :

"store of goods available for sale, distribution or use, esp. goods kept by a trader or shopkeeper ..."

38. According to *Black's Law Dictionary*, "stock" means :

"The goods and wares of a merchant or tradesman, kept for sale and traffic. In a

larger sense, the capital of a merchant or other person, including his merchandise, money and credits, or, in other words, the entire property employed in business."

39. Stroud's Judicial Dictionary (Fifth Edition) defines "stock-in-trade" as under :

"STOCK IN TRADE.--(1) This phrase comprises all such chattels as are acquired for the purpose of being sold, or let to hire, in a person's trade ; but, probably, utensils in a trade are also included in the phrase (*Seymour v. Rapier*, Burb. 28). Setting aside a mere dictum in *Elliott v. Elliott* 11 LJ Ex 3 the only modern authority on the interpretation of this phrase, standing alone, seems to be *Re Richardson* 50 LJ Ch 488. In that case, the testator was a barge-builder and, according to the custom of that trade, he would sometimes, on the sale of a new barge, accept an old one in part payment which he would repair and let out on hire ; at the time of his death he had five of such barges : held, that these barges passed under a bequest of his "stock-in-trade as a barge-builder"."

40. In *Corpus Juris Secundum* (Vol. 83), the following definition finds place :

"The term "stock-in-trade" is very general and it varies in accordance with the business to which it is applied. It is usually applied to the stock of merchants and tradesmen, and includes articles which cover a very wide range, and in general everything that is appropriated or necessary to the carrying on of the trade. In its limited or ordinary meaning, the term applies only to personal property employed by merchants and the like in their trade or business, or, more specifically, to the visible and tangible property with which the trade or business of the owner is carried on, and to which it relates, and it includes all chattels which the merchant acquires and puts into his place of business for use in his trade or for the purpose of sale. It is said to be well understood as meaning goods for sale ; a stock of goods offered for sale ; the goods kept for sale by a merchant or shopkeeper ; a stock of merchandise ; merchandise or goods kept for sale or traffic ; the goods or chattels which a merchant holds for sale."

41. A careful consideration of the aforesaid definitions of the two expressions "expenditure" and "stock-in-trade" makes it abundantly clear that payments made for purchase of stock-in-trade cannot be termed as "expenditure". Money does not go irretrievably in such a case. What is acquired by such payments, namely, stock-in-trade, forms part of the business assets of the assessee. Such assets are sold in due course and the money paid ordinarily recovered with some profit. Stock-in-trade which remains unsold at the end of the year is reflected as assets in the balance-sheet. It is, therefore, difficult to hold the payments made on account of purchase of stock-in-trade as expenditure. Besides, a careful reading of Section 40A(3) also makes it clear that the said section applies only to payments made on account of "expenditure incurred". This is the expenditure which is claimed as deduction in computing the profits and gains of business of the assessee and it is such expenditure which the Assessing Officer may not allow if the conditions set out in the said section are not fulfilled. The result of

disallowance under this section is that the fact of incurring the particular expenditure itself is disregarded. That cannot be so in the case of purchase of assets like stock-in-trade. If such payment is disregarded, then it is difficult to visualise what will happen to the sale price of the goods acquired through such payments if such goods are sold during the year or to the stock of such goods if they remain unsold at the end of the year, whether the factum of sale of such goods can be ignored, whether the profits earned can be disregarded and whether the unsold stock-in-trade can be omitted in computing the value of the business assets of the assessee. The answer is definitely in the negative. Such situations will not arise if a natural meaning is given to the expression "expenditure incurred"--its application is confined and it is not given an artificial meaning so as to extend its application to payments made for acquisition of assets like stock-in-trade.

42. In view of the aforesaid discussion, we are of the clear opinion that Section 40A(3) does not apply to payments made for purchase of stock-in-trade. It is confined only to payments made in respect of the expenditure incurred.

43. Before concluding our discussion, it will be appropriate to refer to the two other reasonings given by the various High Courts in support of their conclusion that purchase of stock-in-trade also amounts to expenditure. One of the reasonings given in support of the wide interpretation to the expression "expenditure" is the legislative intent which was to prevent use of unaccounted money in carrying on business. This approach does not appear to be correct. The law is well settled that the function of the court is to gather the intention of the Legislature from the words used by it and it would not be right for the court to attribute an intention to the Legislature which though not justified by the language used by it, accords with what the court conceives to be reasons for the enactment and then bend the language of the enactment so as to carry out such presumed intention of the Legislature. For the court to do so would be to overstep its limit. In that view of the matter, in our opinion, to give an artificial meaning to the word "expenditure" so as to embrace within it something which, on its normal interpretation, does not fall within it, will be doing violence to the language of the law.

44. We may now revert to the last reasoning. For arriving at the conclusion that expenditure includes purchase of stock-in-trade, the various High Courts also referred to Clauses (f) and (g) of Rule 6DD which lay down the exceptional circumstances under which payments for agricultural produce made in cash might not be disallowed and have used this rule as an aid to the construction of Section 40A(3). We find it difficult to accept this approach. It is well-settled that a statutory rule cannot enlarge the meaning of the section. If a rule goes beyond what the section contemplates, the rule must yield to the statute. The rules should be consistent with the provisions of the Act. Such rules as are not in accordance with the Act are to be inoperative and no effect can be given to them. Courts should not give a forced or unnatural construction upon the

language of the Act in order to bring it in conformity with the rule. Doing so will be like putting the cart before the horse. In case of any inconsistency between a section and the rule made thereunder, the rule must give way to the section. In that view of the matter, in our opinion Rule 6DD cannot be used as an aid to the construction of Section 40A(3) of the Act.

45. In view of the aforesaid discussion, we hold that Section 40A(3) of the Income Tax Act does not apply to payments made for purchase of stock-in-trade as such payments do not amount to payment in respect of expenditure incurred.

46. The question referred, therefore, is answered in the negative and in favour of the assessee.

47. In view of the facts and circumstances of the case, we make no order as to costs.

H.K. Sema, J.

48. I agree.