
(1985) 10 BOM CK 0015

In the Bombay High Court

Case No : Income-tax Reference No.183 of 1975

Commissioner of Income Tax

APPELLANT

Vs

Phalton Sugar Works Ltd.

RESPONDENT

Date of Decision : 24-10-1985

Acts Referred:

Income Tax Act, 1961 — Section 37

Citation : (1986) 52 CTR 158 : (1986) 162 ITR 622 : (1986) 24 TAXMAN 444

Hon'ble Judges : Kania, J;Bharucha, J

Bench : Division Bench

Judgement

Bharucha, J.—Four questions are put to us in this reference u/s 256(1) of the Income Tax Act, 1961, the first two at the instance of the Revenue and the latter two at the instance of the assessee. They read thus :

"(1) Whether, on the facts and in the circumstances of the case, the assessee is entitled to allowance for extra shifts in the same manner as in the years up to 1965-66 ?

(2) Whether, on facts and in the circumstances of the case, the interest attributable to borrowings of the overdraft utilised for payment of dividends is an allowable revenue expenditure ?

(3) Whether, on the facts and in the circumstances of the case, the interest attributable to borrowings of the overdraft utilised for payment of advance tax and/or other taxes is an allowable revenue expenditure ?

(4) Whether, on the facts and in the circumstances of the case, the sum of Rs. 67,299.90 is an allowable revenue expenditure in the assessment of the assessee for the assessment year 1968-69 ?"

2. Counsel are agreed that the first question is covered by the unreported decision of this court in the case of the assessee itself (income tax Reference No. 26 of 1965 decided by Kantawala C.J. and Tulzapurkar J. on July 26, 1974). The

answer to the first question must be, it is agreed, in the affirmative and in favour of the assessee shall be entitled to the allowance in the proportion applicable at the relevant time. Counsel are also agreed that in view of the decision of this court in Commissioner of Income Tax, Bombay City-III Vs. Shree Changdeo Sugar Mills Ltd., the second question must be answered in the affirmative and in favour of the assessment. The first and second questions will, therefore, be so answered without elaboration.

3. The facts that we state now relate to the third question. The assessment year involved is 1968-69, the previous year having ended on September 30, 1967. The assessee had an overdraft bank account. It utilised the overdraft attributed to borrowings on overdraft utilised for payment of taxes was disallowed by the Income Tax Officer, by the Appellate Assistant Commissioner and by the Tribunal on the basis that it was not an allowable revenue expenditure. In so doing, reference was made to order passed in respect of the assessment of the assessee for the assessment year 1969-70 and 1970-71. The Appellate Assistant Commissioner in his order for the assessment year 1969-70 noted that there were huge profit from sale proceeds in the overdraft account on days preceding the payment taxes so that such payment could be attributed to drawings from the assessee's own money deposited in the joint current-cum-cash credit account. In this view, the deposits made in the bank could not be ignored and the payments of tax linked exclusively with the overdraft. The Tribunal set out the state of the overdraft account as it stood at the end of each month during each of the previous years, it was then concerned with and the details of payments of tax in its consolidated order for the assessment years 1969-70 and 1970-71. It found it clear that the assessee had utilised the overdraft for the payment of tax. Accordingly, it reversed the finding of the Appellate Assistant Commissioner.

4. It is not in dispute that interest paid in respect of moneys borrowed for payment of taxes is not a legitimate deduction. It has been so held by this court in Kishinchand Chellaram Vs. Commissioner of Income Tax, Bombay City-III, .

5. What Mr. Kolah, learned counsel for the assessee, argued is based upon the judgment of the Calcutta High Court in Woolcombers of India Ltd. Vs. Commissioner of Income Tax (Central), . Mr. Kolah submitted that deposits in the assessee's overdraft account were sufficient to cover the payments of taxes during the previous year relevant to the assessment year 1968-69 and that, therefore, the presumption was that the taxes had been paid out of such deposits and not out of overdrafts.

6. In Woolcombers of India Ltd. Vs. Commissioner of Income Tax (Central), mentioned above, the assessee had an overdraft account. On December 12, 1969, that is a few days before the end of the assessee's accounting year on December 31, 1969, the account showed a debit balance of Rs. 1,39,412. The assessee paid advance tax of Rs. 18,05,000 on December 15, 1969, which increased the overdraft to Rs. 14,63,593 by December 31, 1969. The Income Tax

Officer disallowed the proportionate interest payable by the assessee to the bank. It was noted by the Appellate Assistant Commissioner that the assessee's entire profit of about rupees twenty-seven lakhs for the year in question had been banked by December 15, 1969, but had not been credited in the overdraft account by that date. It was urged before the Calcutta High Court that where the profits of the assessee's business were sufficient to cover the payment of advance tax during the accounting year, if such amount was paid from a bank account which included the amount of profits as well as the overdraft taken for the purpose of business, the presumption was that the tax was paid out of the profits and not out of the overdraft. It was urged that since the profit for the year in question far exceeded the liability for advance tax, the presumption was that the tax was paid out of the profits for the year and not out of the overdraft, though the profits were put into the overdraft account. Having regard to the aforementioned facts, the Calcutta High Court found that the profits were sufficient to meet the tax liability and that they were deposited in the overdraft account. It was, therefore, presumed that in its essence and true character, the tax had been paid out of the profits of the year and not out of the overdraft account for the running of the business. It was urged by counsel for the Revenue that the particular contention had not been agitated before the Tribunal and that it should not be allowed to be agitated in the reference. The court agreed that had the contention not been urged earlier, it could not be agitated for the first time in the reference, but held that the contention had, in fact, been urged before the Tribunal.

7. The decision in *Woolcombers of India Ltd. Vs. Commissioner of Income Tax (Central)*, was followed by the Calcutta High Court in *Reckitt and Reckitt and Colman of India Ltd. Vs. Commissioner of Income Tax*, and in *Indian Explosives Ltd. Vs. Commissioner of Income Tax*, .

8. Mr. Jetly, learned counsel for the Revenue, contended before us that Mr. Kolah's argument had not been raised before the Tribunal and that it was not open to the assessee to urge it before us.

9. Mr. Kolah's argument requires as its foundation of fact the finding that the assessee's profits for the relevant year were adequate to pay the taxes and that the profits had been deposited in the overdraft account. We find no such finding by the Tribunal in its order for the assessment year 1968-69. Nor do we find in that order any trace of the argument which Mr. Kolah has advanced before us. We must, therefore, hold that it is not open to the assessee to so argue in this reference.

10. It was argued in the alternative by Mr. Kolah that the calculation of interest which was disallowed was defective inasmuch as it had been made upon the state of the overdraft account at the end of each month. In Mr. Kolah's submission, the calculation should have been made on the state of the overdraft account from day to day. It was the Income Tax Officer who made the calculations on the basis of the state of the overdraft account at the end of each

month of the relevant previous year. We find no challenge to this method of calculation. Accordingly, the Tribunal also proceeded upon the basis of the same calculation and we cannot, in the circumstances, find fault with it for having done so.

11. Mr. Kolah submitted, in the last alternative, that the matter should be sent back to the Tribunal for the preparation of a supplementary statement of case in regard to the facts aforementioned. Since the argument itself was not raised before the Tribunal, there was no question of the Tribunal inquiring into the facts which would have formed the foundation of the argument. To send the matter back to the Tribunal to prepare a supplementary statement of case could be tantamount to entertaining an argument not advanced before the Tribunal and asking it to collect evidence anew.

12. In the circumstances, the third question will have to be answered in the negative and in favour of the revenue.

13. This brings us to the fourth question. The facts relevant to this question are, we are afraid, not adequately stated in the statement of case. For a fuller appreciation thereof, we have had to take recourse to the order of the Appellate Assistant Commissioner. The amount of Rs. 67,299.90 referred to in the question was in regard to expense for extra staff engaged by the Maharashtra State Farming Corporation Ltd. for loading and unloading trucks and tractors with sugarcane purchased by the assessee from the MSFC, for the collection of fallen sett is and the salaries and wages of extra staff at the factory gate and contribution to the employee's provident fund for the period November 25, 1964, to May 6, 1965. The amount was covered by five bills of the MSFC. The sugarcane in respect of which these expenses were incurred was purchased by the assessee during 1964-65 season, which fell in the previous year ending September 30, 1965. The assessee did not accept, inter alia, the liability created by the five bills. The dispute regarding them remained unsettled till January 1967, when after discussion with the State authority, it was settled and the assessee accepted liability. Thereupon, the amount of Rs. 67,299 was debited during the previous year with which we are concerned and the Assessee claimed the amount as an allowable deduction for that year. The authorities and the Tribunal disallowed the deduction upon the basis that the liability was known and ascertained earlier and the assessee was not justified in claiming a deduction for it in the year under consideration. Attention was drawn by Mr. Kolah to the judgment of the Supreme Court in Commissioner of Income Tax, Madhya Pradesh, Nagpur and Bhandara Vs. Swadeshi Cotton and Flour Mills Private Ltd., , in support of the proposition that the liability in respect of the amount of Rs. 67,299 having been ascertained only during the previous year in question, it was rightly debited and claimed as a deduction in the assessment for that year. The case before the Supreme Court was in respect of a claim for bonus. The assessee followed the mercantile system of accounting. It was held, after a discussion of various judgments, that workmen were entitled to make a claim to bonus only

after certain conditions were satisfied; that the claim had to be made from year to year; that it had to be either settled amicably or by industrial adjudication; and that, if there was a loss or no claim was made, no bonus was permissible. In the Supreme Court's opinion it was only when the claim to liability was incurred by an assessee who followed the mercantile system of accounting. On the facts of the case before the Supreme Court, it was clear that it was only in 1949 that the claim for bonus was settled by an award of the Industrial Tribunal and, therefore, the only year to which the liability could be properly attributable was the year 1949.

14. In *SETH CHAMPALALji RAMSWARUP, BEAWAR Vs. COMMISSIONER OF Income Tax, U.P. and V.P.*, , the Allahabad High Court was concerned with a case in which the assessee had received solicitor's bills. It was held that until the time when, during the assessment year in question, the bills were finally settled and the amount reduced to less than half, the liability of the assessee had not been finally determined. It was only then that the liability for payment of the bills accrued against the assessee. Accordingly, the expenditure of about Rs. 24,000 thereon pertained to the relevant assessment year.

15. In *Swadeshi Cotton Mill Co. Ltd. Vs. Commissioner of Income Tax*, , the Allahabad High Court, relying inter alia, upon the judgment of the Supreme Court earlier quoted, drew a distinction between a statutory liability and a liability based upon a contractual obligation. In the case of a statutory liability, the quantification or ascertainment could not postpone the accrual thereof; but if the liability was based on a contractual obligation, it arose only when it was ascertained. In the case before the Allahabad High Court, the assessee company followed the mercantile system of accounting. In its assessment for the assessment year 1960-61, it claimed deduction of a certain sum paid to a research association towards its annual contribution for the year ended March 31, 1958. There had been some dispute between the assessee and the research association with regard to the concerned bill. The payment was ultimately made in the previous year relevant to the assessment year 1960-61. It was held that the liability accrued in the previous year relevant to the assessment year 1960-61 and the claim of the assessee was allowed.

16. Mr. Jetly, learned counsel for the Revenue, submitted that unless the expense had been incurred in the relevant previous year, it was not allowable revenue deduction for the assessment year concerned. He relied upon the judgment of this court in *Commissioner of Income Tax, Madhya Pradesh Vs. Central Provinces Manganese Ore Co. Ltd.*, . This court there held that if a statutory liability arose in a particular year, then, an assessee maintaining his books of account on mercantile arose notwithstanding the fact that he was taking steps to dispute his liability and had committed himself to make entries in respect thereof in his books of account.

17. The question before us is not whether an assessee, maintaining books of account on the mercantile system, is entitled to claim deduction in the year in

which the liability arose notwithstanding the fact that he was disputing his liability, but whether it is open to such an assessee to claim the deduction not in the year in which the liability arose but in the year in which the dispute about it was finally adjudicated upon or settled. The judgment of the Supreme Court in Commissioner of Income Tax, Madhya Pradesh, Nagpur and Bhandara Vs. Swadeshi Cotton and Flour Mills Private Ltd., and the two judgments of the Allahabad High Court referred to above provide a pointer. In our view, where a liability arising out of a contractual obligation is disputed, the assessee is entitled, in the assessment year relevant to the previous year in which the dispute is finally adjudicated upon or settled, to claim a deduction in that behalf.

18. In the instant, case, the assessee disputed its liability in regard to the five bills of the Maharashtra State Farming Corporation Ltd. The liability was settled only during the previous year relevant to the assessment year 1968-69. The assessee was entitled to seek a deduction in respect of the liability in its return for the assessment year 1968-69.

19. The fourth question put to us must, therefore, be answered in the affirmative and in favour of the assessee.

20. To conclude, the answers to the questions are as follows :

Question No. 1 : In the affirmative and in favour of the assessee; the assessee shall be entitled to the allowance in the proportion applicable at the relevant time.

Question No. 2 : In the affirmative and in favour of the assessee.

Question No 3 : In the negative and in favour of the Revenue.

Question No 4 : In the affirmative and in favour of the assessee.

21. There shall be no order as to costs.