

(1979) 11 MAD CK 0025
In the Madras High Court
Case No : T.C. No. 279 of 1976

Commissioner of Income Tax

APPELLANT

Vs

Planters Co. (P.) Ltd.

RESPONDENT

Date of Decision : 14-11-1979

Acts Referred:

Income Tax Act, 1961 — Section 256(1), 41(1)

Citation : (1980) 15 CTR 395 : (1980) 123 ITR 648

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

Bench : Division Bench

Advocate : A.N. Rangaswami and Nalini Chidambaram, for the Appellant; K.J. Rebello, for the Respondent

Judgement

Sethuraman, J.—The Appellate Tribunal has referred the following question u/s 256(1) of the Act:

Whether, on the facts and in the circumstances of the case, the Appellate Tribunal was right in holding that the excess sales tax realised by the

assessee during earlier years and transferred to the credit of profit and loss account on June 30, 1970, constituted trading receipt of the years in

which it was received and consequently it cannot be assessed to tax in the year of assessment for 1971-72 ?

2. The assessee, a private limited company, is carrying on business in sale of tea. When orders for supply of tea were received from buyers,

invoices were prepared for the sale price mentioned in the orders, and sales tax was separately charged and added in the invoices. The value of tea

sold was separately credited to the "tea sales account" and the sales tax collected was credited to the "sales tax reserve account" in the general

ledger. The collection of sales tax for the years 1955 to 1959 was credited to this

account and the payments throughout were debited. The excess in the said account came to Rs. 33,097.13 which was kept on between June 30, 1960, and June 30, 1969, in the same account. The assessee credited this sum to the profit and loss account as on June 30, 1970. The ITO assessed the said sum of Rs. 33,097.13 as the income of the assessee liable to be taxed in the assessment for the assessment year 1971-72. The AAC, on appeal, held that the said sum formed part of the turnover and it, therefore, constituted the assessee's income and that the ITO was, accordingly, justified in assessing the sum for the assessment year 1971-72. The assessee appealed to the Tribunal. It held that since the excess sales tax realised related to the assessment years 1954-55 to 1958-59, it could constitute trading receipts only for those years and, consequently, it could be assessed to Income Tax only in those years and not in the year 1971-72. The contention of the revenue that the income accrued to the assessee in this year when the amount was transferred to the profit and loss account was negated by holding that the accrual of income did not depend upon whether the assessee chose to make the entries in the accounts and transfer the same to the profit and loss account or not. A contention was taken before the Tribunal that Section 41(1) of the Act could be applied for assessing the said amount. The Tribunal pointed out that the section enabled the revenue to treat as income what had earlier been allowed as deduction, and that when no allowance had been granted in any year in respect of the sum of Rs. 33,097.13, the condition precedent for invoking Section 41(1) was absent. The result was that the sum of Rs. 33,097.13 was excluded from the assessment. The Commissioner has challenged the correctness of the Tribunal's conclusion on this aspect.

3. It is clear from the statement of the case drawn up by the Tribunal that the sum of Rs. 33,097.13 was the collection between the years 1955 and 1959 and that it had not been allowed as deduction as and by way of sales tax paid or payable in any year so far. The question that now arises for consideration is whether the said sum could be brought to tax in the year 1971-72 merely by reason of the transfer entry made by the assessee.

4. Income is liable to be taxed on the basis of its accruing or arising to the assessee or its receipt by the assessee, during the relevant previous year.

The accrual or arising of the income is generally dependent on the method of accounting employed by the assessee. In the cash system of accounting, the accrual or arising of the income will be simultaneous with its receipt. In the mercantile system of accounting, the accrual of the income is independent of its receipt. So long as the amount is due to the assessee, the system of accounting would envisage the amount being treated as having accrued to the assessee. In the present case, the system of accounting employed by the assessee is mercantile. The amounts were realised between 1955 and 1959 and they were thus accountable in those years.

5. We have now to examine the character of the amount in order to find out whether it is income and has accrued to the assessee. As far as the sale price is concerned, there can be no dispute that it is a trading receipt and that it accrues at the time when the sale is effected in the mercantile system of accounting. The question as regards the character of sales tax collected by the assessee at the time of effecting the sales has been considered by the Supreme Court in *Chowringhee Sales Bureau (P) Ltd. Vs. Commissioner of Income Tax, West Bengal*. In that case, the assessee was a private limited company dealing in furniture. It acted also as an auctioneer. During the relevant year, the assessee realised Rs. 32,986 as sales tax and credited it separately in its account books under the head "Sales tax Collection Account". The amount was not paid to the sales tax authorities or to the actual owner of the goods which were auctioned. The assessee took up the position that the statutory provisions creating a liability to tax in respect of such receipts as and by way of tax was not valid. The result was that the assessee did not pay the amount to the State Government as and by way of sales tax. The assessability of the collection of Rs. 32,986 came up for consideration of the Supreme Court and it was held that the amount realised as sales tax by the assessee in its character as an auctioneer formed part of its trading or business receipts and that the fact that the assessee credited the amount received under the head "Sales tax collection account" did not make any material difference. The Supreme Court pointed out that the true nature and quality of the receipts, and not the head under which it is entered in the account books, would be decisive and that if a receipt was a trading receipt, the fact that it is not so shown in the account books of the assessee

would not prevent the assessing authority from treating it as trading receipt. It was also pointed out that the assessee would be entitled to claim

deduction of the amount paid as sales tax, as and when it was paid to the State Government. This decision has been applied by this court and the

other decisions on this point have also been noticed in Commissioner of Income Tax Vs. E.A.E.T. Sundararaj, . It is unnecessary to dilate further

on this point.

6. The character of the amount is thus fixed as a trading receipt and that too, of the year in which it was received. The fact that it was credited to a

separate account did not in any manner affect its quality or character as a trading receipt. When once this quality of the receipt is determined, then

it would have to be assessed only in the year in which it was collected: The assessee, of course, would be entitled to claim deduction for the amount

paid as sales tax and the deduction would have to be allowed in the year in which the liability is created or the amount is paid to the sales tax

authorities, as the case may be.

7. The next question that arises is whether, even though the amount was a trading receipt of the year in which it was collected, still, by reason of the

amount having been appropriated and transferred by the assessee to the profit and loss account, the character of the receipt is changed in any

manner. On this aspect, there is an instructive decision of the Court of MORLEY (INSPECTOR OF TAXES) Vs. TATTERSALL., . In that

case, the assessee was a firm of auctioneers who did business in the sale of horses. During a long period, owing to the fact that several sellers of

horses failed to claim the balances of purchase monies due to them, large unpaid balances had been accumulated by the firm. By a clause in the

articles of the existing partnership deed, it was provided that all unclaimed balances existing on December 31 in the year of account succeeding the

six year period prior to it should be transferred to the credit of the partners in the proportions to which the partners were entitled. By another

clause in the deed, it was provided that notwithstanding any transfer of such unclaimed balances, all liabilities subsisting in reference to the balances

should continue to be borne by the partners. The firm was assessed to Income Tax in respect of unclaimed balances transferred to the current

account of the partnership in a particular year. The firm contended that the

unclaimed balances did not at any time become profits or trading receipts, and that they were always to be considered as liabilities, for the statute of limitations did not apply to the case. It was held that the quality and nature of a receipt for Income Tax purposes were fixed once and for all when the subject of the receipt was received, and that, consequently, as the unclaimed balances, when first received, were obviously liabilities, no subsequent operation could turn them into trading receipts. It was, therefore, held that they were not assessable to Income Tax. At page 323, Greene M.R. pointed out:

It seems to me that the quality and nature of a receipt for Income Tax purposes is fixed once and for all when it is received. What the partners did

in this case, as I have said, was to decide among themselves that what they had previously regarded as a liability of the firm they would not, for

practical reasons, regard as a liability; but that does not mean that at that moment they received something, nor does it mean that at that moment

they imprinted upon some existing asset a quality different from what it had possessed before. There was no existing asset at all at that time. All that

they did, as I have already pointed out, was to write down a liability item in their balance-sheet, and how in the world by effecting that operation

you can be said to have converted a sum received years and years ago into something which it never was, is a thing which, with all respect, passes

my comprehension.

8. These words are apt to cover the point raised in the present case with particular reference to the transfer entry. In other words, these amounts

were received during 1955 and 1959 as trading receipts. The result of the transfer to the profit and loss account is merely to close that particular

account. But that did not, in any manner, affect either the rights of the assessee or his obligation to the tax department. It is not possible to attribute

to the entry- a power to transmute a trading receipt of an earlier year into income of this year. There has been no accrual of "any income by reason

of the transfer entry being made from the sales tax account to the profit and loss account of this year. In fact, in the years in which these amounts

were received, they should have been credited to the trading account or the sales account and they would have featured in the same way as sale

proceeds realised from the parties. The result is that they would have been taxed

in those years. If they were not taxed for any reason whatsoever, that cannot affect in any manner the question before us. The question is whether the said amounts are liable to be taxed in this year, as if the

amounts have accrued in this year. The answer is "no". The omission to tax them in the earlier years affords no ground for taxing them in this year.

9. The learned counsel for the Pioneer Consolidated Co. of India Ltd. Vs. Commissioner of Income Tax, , to support the stand of the revenue in

the present case. In that case, the assessee was carrying on the business of clearing and forwarding agents. The assessee received various amounts

from its constituents for incurring expenses for and on behalf of the constituents. The total sum received was Rs. 29,643 and it was lying in the

books of the company to the credit of the constituents up to 1960-61, from some earlier years. Those amounts were not claimed by the respective

constituents and during the relevant accounting year, the assessee transferred the amount to the credit of the profit and loss account. The ITO

assessed this amount as income and this was the subject-matter of the reference to the High Court in the said decision. The Allahabad High Court

pointed out at page 412, as under :

So long as those sums represented deposits in favour of the constituents, the sums could not be treated as income of the assessee. It was only

during the relevant accounting year that the sum of Rs. 29,643 was transferred from the deposit account to the profit and loss account. It was at

this stage that the amount assumed the character of income of the assessee. The Tribunal was right in holding that the sum of Rs. 29,643

represented income of the assessee for the assessment year 1962-63.

10. We have already referred to the decision of the Court of Appeal in *Morley (Inspector of Taxes) v. Tattersail* [1939] 1 ITR 316. That decision

has not been cited or noticed in the Allahabad case. It would, in one view, be necessary to see if the principle laid down in this decision requires

reconsideration in the light of the principle set out in the decision of the Court of Appeal. However, it is unnecessary for us to make any further

comment about the decision except to say that the said decision does not cover the problem now before us. In the said decision, the amounts were

actually received by the assessee for the purpose of incurring certain expenses on behalf of its constituents. Therefore, at the point of receipt, they

were not treated as trading receipts. They were accountable to third parties. Only when appropriated they became income. In the present case,

they were trading receipts, even in the year of receipt, as pointed out by the Supreme Court in Chowringhee Sales Bureau (P) Ltd. Vs.

Commissioner of Income Tax , West Bengal, . The transfer to the profit and loss account in this case is bereft of significance. Therefore, the

Allahabad High Court's decision would have no scope for application to the facts before us. The result is, the question referred to us is answered

in the affirmative and in favour of the assessee. The assessee will be entitled to its costs. Counsel's fee Rs. 500.