
(1997) 12 MAD CK 0062

In the Madras High Court

Case No : T.C.P. No. 970 of 1993 (Revision No. 558 of 1993)

Hariharaputhra Plantations Ltd.

APPELLANT

Vs

State of Tamil Nadu

RESPONDENT

Date of Decision : 01-12-1997

Acts Referred:

Income Tax Act, 1961 — Section 10(1), 10(2), 28

Citation : (1999) 240 ITR 201

Hon'ble Judges : K.P. Sivasubramaniam, J; Janarthanam, J

Bench : Division Bench

Advocate : Deokinandan, for the Appellant; K.M.L. Majele, for the Respondent

Judgement

Janarthanam, J.—This revision, at the instance of the assessee - Hariharaputhra Plantations Ltd., Netta P. O., Kanyakumari District, is

directed against the order dated January 29, 1993, of the Tamil Nadu Agricultural Income Tax Appellate Tribunal, Madras-104 (for short "the

Tribunal"), and made in A.T.A. No. 48 of 1990 relatable to the assessment year 1989-90 as respects the income derived from agriculture under

the provisions of the Tamil Nadu Agricultural Income Tax Act, 1955 (Tamil Nadu Act No. V of 1955 - for short "the Act").

2. The assessee-company, it appears, owns 130-50-0 hectares of rubber plantations in Kalial village. In the process of computation of agricultural

income for the said year, the claims made by the assessee for deduction of certain alleged expenses are relatable to soil conservation in a sum of

Rs. 1,32,043, domestic inquiry legal expenses to the tune of Rs. 750 and commission paid on sales of latex in a sum of Rs. 11,140.04, all totalling

to Rs. 1,43,933.04.

3. The Assessing Officer, namely, the Agricultural Income Tax Officer-I, Nagercoil (Assessing Officer) as well as the Assistant Commissioner of

Agricultural Income Tax, Grade-I, Nagercoil (Appellate Authority), and also the Tribunal, disallowed the claims so made by the assessee-

company, culminating in the present action - Tax Case (Revision) No. 970 of 1993.

4. From the submissions of Mr. K. J. Chandran, learned counsel appearing for the assessee-company, and Mr. K. Elango, learned Government

Advocate (Taxes) representing the Revenue, the one and the only question that crops up for consideration is as to :

Whether the concurrent findings recorded by all the taxing authorities below, inclusive of the Tribunal that the assessee-company is not entitled to

claim by way of deduction in the computation of agricultural income the alleged expenditure incurred under the various heads, such as ""soil

conservation"", ""domestic inquiry"" and ""commission paid on sale of latex"" amounting to Rs. 1,43,933.04, on the facts and in the circumstances of

the case, are sustainable in law ?

5. There is no pale of controversy that the assessee-company had been following the ""mercantile system of accounting"".

6. As respects the claim of deduction relatable to ""soil conservation"" expenses amounting to Rs. 1,32,043 the finding recorded by all the authorities

below, inclusive of the Tribunal is that a provision, that is to say, a ""budgetary allocation"" in a sum of Rs. 1,32,043 for ""soil conservation"" purposes

had been made and that is all and nothing further. To put it otherwise, it is not as if the expenditure in a huge sum, as stated above, had been

incurred by the assessee-company and thereby a liability was created in that regard and the liability so created remains to be discharged by

postponing the payment of the actual amount in a subsequent year. On a sort of a reasoning of this kind, the authorities below, inclusive of the

Tribunal, disallowed the claim and such sort of a rationale or reasoning adopted by them cannot at all be found fault with, on the facts and in the

circumstances of the case. On a factual matrix of this nature, we rather feel that we can straightaway, hold that the disallowance, as made by the

authorities below under this head, rather reflects the real legal position and, therefore, no interference need be made.

7. We are, however, impelled : to refer to certain decisions or precedents, as cited by learned counsel for the assessee-company, inasmuch as the said learned counsel feels that the findings so recorded by the authorities below cannot at all be supported, on the face of the precedents, he had relied upon.

8. Out of the four precedents relied upon by the said learned counsel, two of them are relatable to the distinction between "cash system of accounting" and ""mercantile system of accounting"". We may relate them now.

9. In *Indermani Jatia Vs. Commissioner of Income Tax, Uttar Pradesh*, , what their Lordships of the Supreme Court expressed at the relevant paragraph at pages 302-303 is as below :

It is well-known that the mercantile system of accounting differs substantially from the cash system of book-keeping. Under the cash system, it is

only actual cash receipts and actual cash payments that are recorded as credits and debits; whereas, under the mercantile system, credit entries are

made in respect of amounts due immediately they become legally due and before they are actually received; similarly, the expenditure items for

which legal liability has been incurred are immediately debited even before the amounts in question are actually disbursed. Where, accounts are

kept on mercantile basis, the profits or gains are credited though they are not actually realised and the entries thus made really show nothing more

than an accrual or arising of the said profits at the material time. The same is the position with regard to debits made.

10. In *Morvi Industries Ltd. Vs. Commissioner of Income Tax (Central) Calcutta*, , their Lordships of the Supreme Court followed the earlier

decision rendered in *Indermani Jatia Vs. Commissioner of Income Tax, Uttar Pradesh*, relatable to the finer aspects of distinction and difference

between ""cash system of accounting"" and ""mercantile system of accounting"".

11. Implicit reliance had also been placed by the said learned counsel on two more precedents emerging from the apex court of this country to

drive home the point that where the expenditure is actually incurred and thereby a liability is created; but there is postponement of the payment of

the liability so created, it can figure as an allowable deduction in the computation of income of the year, in case the system of accounting followed

by the assessee was one of ""mercantile system of accounting"".

12. In *Calcutta Company Ltd. Vs. The Commissioner of Income Tax, West Bengal*, the appellant bought the lands and sold them in plots fit for

building purposes undertaking to develop them by laying out roads, providing a drainage system and installing lights, etc. When the plots were sold,

the purchaser paid only a portion of the purchase price and undertook to pay the balance in instalments. The appellant in its turn undertook to

carry out the developments within six months but time was not of the essence of the contract.

13. In the relevant accounting year, the appellant actually received in cash only a sum of Rs. 29,392 towards sale price of lands, but in accordance

with the mercantile system of accounts adopted by it, it credited in its accounts the sum of Rs. 43,692 representing the full sale price of lands. At

the same time, it also debited an estimated sum of Rs. 24,809 as expenditure for the developments it had undertaken to carry out, even though no

part of that amount was actually spent. The Department disallowed the said expenditure.

14. In such a context, the Supreme Court held :

That the undertaking to carry out the developments within six months from the dates of the deeds of sale (which, in view of the fact that time was

not of the essence of the contract, meant a reasonable time) was unconditional, the appellant binding itself absolutely to carry out the same. That

undertaking imported a liability on the appellant, which accrued on the dates of the deeds of sale, though that liability was to be discharged at a

future date. It was thus an accrued liability and the estimated expenditure which would be incurred in discharging the same could be deducted from

the profits and gains of the business, and the amount to be expended could be debited in accounts maintained in the mercantile system of

accounting before it was actually disbursed. The difficulty in the estimation thereof did not convert the accrued liability into a conditional one,

because it was always open to the Income Tax authorities concerned to arrive at a proper estimate thereof having regard to all the circumstances

of the case.

That the sum of Rs. 24,809 represented the estimated amount which would have to be expended by the assessee in the course of carrying on its

business and was incidental to the business and, having regard to the accepted

commercial practice and trading principles, was a deduction which, if there was no specific provision for it, u/s 10(2) of the Income Tax Act, was certainly an allowable deduction, in arriving at the profits and gains of the business of the appellant, u/s 10(1) of the Act, there being no prohibition against it, express or implied, in the Act.

15. The expression "profits or gains" in section 10(1) of the Income Tax Act has to be understood in its commercial sense and there can be no

computation of such profits and gains until the expenditure which is necessary for the purpose of earning the receipts is deducted therefrom -

whether the expenditure is actually incurred or the liability in respect thereof has accrued even though it may have to be discharged at some future

date.

16. In Commissioner of Income Tax Vs. Cawnpore Textiles Ltd., , the assessee was maintaining ""mercantile system of accounting"". Bonus in the

relevant assessment year was declared and in fact provision was made in the balance-sheet. Actually payment was, however, made in the

subsequent year.

(a) The question that arose therein was, as to whether the assessee was entitled to deduction in the year in which provision has been made.

(b) In answering the question, the Allahabad High Court held (headnote) :

The Tribunal was correct in holding that the liability for payment of bonus accrued due on the dates on which the provision was made in the

balance-sheet of the assessee-company for the three years under appeal irrespective of the fact that the sums were actually paid in subsequent

years. Under the mercantile system of accounting, liability accrues on the date when the obligation to pay arises and the obligation arose in the

present case when the board of directors passed the resolution declaring bonus and the relevant entry was made in the account books providing

for bonus.

17. The two decisions, as referred to above, we are of the view, cannot render a helping hand to the assessee, in the sense of getting necessary

relief of the allowance of the claim made for ""soil conservation"" work, on the peculiar facts and circumstances of the instant case.

18. It is not as if, as we have already stated, the assessee-company actually incurred the expenditure on ""soil conservation"" during the relevant

assessment year and a liability thereof had been created and the liability so created was postponed for payment in subsequent years. It is, we are able to perceive from the findings as well as the records produced for our perusal by learned Government Advocate (Taxes) representing the Revenue that the assessee-company, after all, made a provision, rather to say ""a budgetary provision"" for the incurring of such an expenditure and nothing further. In such circumstances, it cannot at all be stated that a liability, in fact, had been created, so that there was any sort of an obligation to pay on the part of the assessee-company at a future point of time. In such a situation, even though the assessee-company had been adopting the system of mercantile accounting, it cannot be expected to have the relief of the claim of deduction of an expenditure, for which budgetary allocation alone had been made, as we have stated earlier. In those two decisions, on which implicit reliance had been placed by the said learned counsel, the actual liability accrued during the relevant assessment year and an obligation had been created on the part of the concerned assessee to discharge that obligation so accrued in subsequent assessment years. In this view of the matter, we are of the view that the authorities below, inclusive of the Tribunal, were right in rejecting the claim of allowance made by the assessee-company relatable to ""soil conservation"" amounting to Rs. 1,32,043.

19. The second claim is relatable to the disallowance made by the authorities as respects the expenses incurred by the assessee-company, in holding a domestic inquiry. It appears, an employee of the assessee-company committed certain petty thefts of goods or articles. The assessee-company, instead of lodging a FIR before the police in relation to the thefts so committed, actually held a domestic inquiry and for the conduct of the domestic inquiry, a fee in a sum of Rs. 750 had been paid to an advocate. The claim so made had been disallowed on the flimsy ground of holding directly a domestic inquiry, instead of lodging an information to the police. To such a view, we are unable to affix our seal of approval. It is always open to the assessee-company to either lodge an information to the police in respect of petty thefts committed by its employees during their employment or hold a domestic inquiry and take disciplinary action against the offending employee without even lodging an information before the police. The fact that the assessee-company incurred an expenditure of Rs. 750 by payment of fees to the advocate was not at all denied. Such

being the case, we can safely take it for granted that the said sum had been actually expended by the assessee-company.

20. The question is whether the said expenses had any sort-of a nexus or link relatable to "agriculture". "Agriculture" has more or less developed as an "industry" in modern times. The agricultural operation will have to be managed by employment of necessary staff, apart from engaging labourers for actually tilling the soil and deriving income therefrom. The salaries and allowances paid to staff members are allowable as an expenditure, having nexus or link with agriculture and on this aspect of the matter, the apex court of this country expressed its views on occasions more than one that the expenditure incurred for holding a domestic inquiry in respect of petty thefts committed by the employees of an assessee-company on the same analogy or reasoning have to be allowed as expenditure incurred pertaining to "agriculture". In cases of thefts of goods of agricultural produce, if action is not taken, it would give rise to recurrence of commission of such thefts affecting agriculture itself. Therefore, it cannot be stated that the expenses incurred for holding domestic inquiry are not having any nexus or link with agricultural operations. In this view of the matter, we are of the view that the expense incurred by the assessee-company in a sum of Rs. 750 for holding domestic inquiry in respect of certain thefts committed by its employee is certainly an allowable expenditure in computing the agricultural income of the assessee-company during the relevant assessment year.

21. What is left out of consideration is the commission paid on sales of latex, which amounts to Rs. 11,140. All the authorities below, inclusive of the Tribunal, as stated earlier, disallowed such a claim, on the ground that the commission paid on the sale of latex cannot at all be construed as an expenditure incurred in deriving the income from agriculture. The view so held by the authorities below cannot at all be stated to be incorrect or wrong, on the facts and in the circumstances of the case.

22. Admittedly, the assessee-company owns an estate, having rubber plants. The income from the estate is income by way of rubber latex. Any amount spent by the assessee-company for deriving the income from rubber plants can alone figure as deduction in computing the income derived by the assessee-company from such rubber plantations. Here the expenses

admittedly are relatable to commission paid on the sales of latex, an agricultural produce. This sort of a commission paid, learned counsel appearing for the assessee-company would say, can very well figure as a deduction u/s 5(e) of the Act.

23. Section 5(e), as it then stood - that is to say, before the amendment by Tamil Nadu Act No. LVI of 1994 - reads as under :

5. Computation of agricultural income. - The agricultural income of a person shall be computed after making the following deductions, namely :-

....

(e) any expenditure incurred in the previous year (not being in the nature of capital expenditure or personal expenses of the assessee) laid out or expended wholly and exclusively for the purpose of the land;

24. If we scan or analyse provisions, as extracted above, it is crystal clear that the parameters are as below, namely,

(i) expenditure ought to have been incurred in the previous year;

(ii) the expenditure so incurred should not be in the nature of a capital expenditure or personal expenses of the assessee; and

(iii) the expenditure incurred in the previous year must be laid out or expended wholly and exclusively for the purpose of the land.

25. The expression ""wholly and exclusively for the purpose of the land"" had been subjected to interpretation by us on occasions more than one and

also by the apex court. ""Wholly and exclusively for the purpose of the land"" had been interpreted that the expenses must be laid out or expended

for the purpose of the land, from which the net income had been derived. By no stretch of imagination, it can be stated that the commission paid for

the sale of latex of agricultural produce is stated to be an expense incurred for the purpose of the land from which the net income is derived. It

partakes of the character or colour of the expenses incurred for the sale transaction of the agricultural latex only. Even if the assessee-company

incurred such expenditure by making payment to the commission agent, even then the assessee-company is not entitled to a deduction for the

reasons, we have stated above. This apart, as a matter of fact, the assessee-company, it appears, did not produce any voucher before the

authorities evidencing the payment of any amount by way of commission to the commission agent or any other evidence for incurring a liability

therefor, so that the liability so incurred was to be discharged at a future point of time. In this view of the matter, the commission paid on sale of

latex cannot at all be allowed as a deduction in the computation of the income of the assessee-company. The authorities below, inclusive of the

Tribunal, rightly rejected the claim made in that regard.

26. In view of our finding as relatable to the expenses incurred by the assessee-company by way of payment of fees to an advocate for holding

domestic inquiry", the orders of the Tribunal as well as the authorities below, namely, appellate authority and the Assessing Officer, require to be

modified in that regard. The Assessing Officer is, therefore, directed to give relief to the assessee-company therefor.

27. The revision, in other respects, shall stand dismissed. No costs.