
(1980) 10 MP CK 0015
In the Madhya Pradesh High Court
Case No : M.C.C. No. 493 of 1976

Trikamlal

APPELLANT

Vs

Commissioner of Income Tax

RESPONDENT

Date of Decision : 24-10-1980

Acts Referred:

Citation : (1982) 134 ITR 450

Hon'ble Judges : R.K. Vijayvargiya, J;G.G. Sohani, J

Bench : Division Bench

Advocate : G.M. Chaphekar, for the Appellant; S.C. Bagadiya, for the Respondent

Judgement

Sohani, J.—By this reference u/s 256(1) of the I.T. Act, 1961 hereinafter called the Act, the Income Tax Appellate Tribunal, Indore Bench, has referred the following questions of law to this court for its opinion:

" 1. Whether, on the facts and in the circumstances of the case, the Tribunal has correctly held that the receipt of Rs. 24,000 is not in the nature of a capital receipt ?

2. Whether the Tribunal has correctly held in law that, on the facts and in the circumstances of the case, the profit of Rs. 24,000 accrued in the assessment year 1962-63 and not in the years 1944 to 1947 ?

3. Whether, on the facts and in the circumstances of the case, the Tribunal has correctly held that-

(a) the receipt of Rs. 24,000 is chargeable to tax u/s 28 of the Income Tax Act, 1961, on the footing that the same cloth business is still continued by the assessee ; and

(b) as a corollary the amount was taxable in the A.Y. 1962-63, on mercantile system of accounting which was followed for the cloth business when carried on in proprietary capacity and not on cash basis in the assessment year 1963-64, when the amount was received and credited in the assessee's capital account? "

2. The material facts giving rise to this reference briefly are as follows : The assessee is an individual deriving income from property and from business carried on by M/s. Surendra Narendra, a firm of which the assessee was a partner at the material time. The assessment year in question is 1962-63. The assessee had initially filed a return disclosing a loss of Rs. 7,190. The assessment was framed on a total net loss of Rs. 141. Subsequently, while, the books of account of the firm, M/s. Surendra Narendra were being examined for the assessment of that firm for the assessment year 1963-64, the ITO noticed a credit of Rs. 24,000 in the accounts of the assessee on 10th September, 1962. The ITO, therefore, reopened the assessment of the assessee for the assessment year 1962-63. The ITO found that the circumstances in which the amount of Rs. 24,000 was received by the assessee on 10th September, 1962, were these: The assessee was carrying on business in cloth from the year 1939-40. Under the provisions of the Cotton Control Order, 1943, the assessee was allotted a quota of 180 bales of cloth per quarter beginning from 1st June, 1944, from Nazarali Mills, Ujjain. However, the Nazarali Mills supplied to the assessee only 780 bales of cloth during the period from 1st June, 1944, to 31st August, 1947. On account of this short supply of bales of cloth, the assessee filed a suit against the Mills in the Court of the District Judge, Ujjain, on 16th September, 1947, claiming compensation. A decree for a sum of Rs. 30,000 was passed by the district judge in favour of the assessee on 20th June, 1961. However, a compromise was arrived at between the assessee and the Nazarali Mills, and a sum of Rs. 24,000 was received by the assessee on 10th September, 1962, in full and final settlement of the decretal amount. The compromise was recorded by the First Additional District Judge, Ujjain, on 15th September, 1962, and the execution case was dismissed.

3. On behalf of the assessee, two contentions were raised before the ITO. It was urged that the receipt of Rs. 24,000 pertained to a period from 1944 to 1947 when there was no Income Tax in force at Ujjain and that the nature of the receipt was that of a capital receipt. It was also contended that the business, in respect of which compensation was received by the assessee, was closed and that the assessee was no longer carrying on that business. The ITO rejected both these contentions. He held that as the amount of compensation was received by way of damages for a breach of contract, it was in the nature of a revenue receipt. It was further held that the income in question accrued to the assessee when the assessee acquired the right to receive that amount on 20th June, 1961 when the Additional District Judge, Ujjain, passed a decree in favour of the assessee in C.S. No. 28 of 1949. The ITO further held that the amount received by the assessee was in the nature of revenue receipt and was chargeable to tax and that it was immaterial whether the business in respect of which compensation was received by the assessee was or was not carried on by the assessee during the assessment year in question. Aggrieved by the order passed by the ITO, the assessee preferred an appeal before the AAC. Before the AAC, it was again urged that the amount of compensation should be held to be the

income of the assessee for the period from 1st June, 1944, to 31st August, 1947, and that prior to the accounting year relevant to the assessment year 1962-63, the assessee had discontinued his cloth business. The AAC held that the assessee became entitled to receive the amount in question on 20th June, 1961, when the decree was passed in his favour. It was further held that the assessee was carrying on business in cloth under the name and style of M/s. Surendra Narendra and was assessed as a proprietor of that business till 23rd October, 1957, and that since that date the assessee had entered into a partnership agreement with his son to carry on the same business under the name and style of M/s. Surendra Narendra. In view of these facts, the AAC held that the business of cloth carried on by the assessee in the past was continued by him during the assessment year in question. In this view of the matter, the AAC dismissed the appeal preferred by the assessee. On further appeal, it was contended before the Tribunal that for taxing the profits and gains of a business u/s 28 of the Act, a business must be in existence and carried on by the assessee himself in the same status, and the business of the firm could not be held to be the same as the individual business of the assessee. The Tribunal found that the assessee was carrying on business in cloth in the assessment year in question in partnership with his son and hence he would be held to be carrying on the old cloth business in respect of which the amount of compensation was received by him. The Tribunal also negatived the contention that the income in question had accrued to the assessee in the years 1944 to 1947. The Tribunal held that the assessee followed the mercantile system of accounting and hence the ITO was justified in assessing the income in question on accrual basis. The Tribunal, therefore, dismissed the appeal. Aggrieved by the order passed by the Tribunal, the assessee submitted an application for making a reference and it is at the instance of the assessee that the aforesaid questions of law have been referred to this court for its opinion.

4. Shri Chaphekar, learned counsel for the assessee, contended that the amount of Rs. 24,000 had become due to the assessee from the Nazarali Mills in the years 1944 to 1947 and that the said amount was received in respect of a business which the assessee had ceased to carry on during the assessment year in question. It was urged that the assessee was, during the years 1944 to 1947, carrying on the business of dyeing in Nazarali Mills, Ujjain, and that the said business was not carried on by the firm, of which the assessee was a partner, during the assessment year 1962-63. It was urged that the Tribunal had not applied its mind to this aspect of the question, and a finding be, therefore, called by directing the Tribunal to send a supplementary statement of case. It was further contended that the Tribunal erred in holding that the income of Rs. 24,000 had accrued to the assessee in the assessment year 1962-63. In reply, Shri Bagadiya, learned counsel for the department, contended that the Tribunal had found that the assessee was maintaining the accounts on mercantile basis and that the right to receive the amount of compensation had accrued to the assessee in the assessment year 1962-63, when the decree was passed in his

favour. It was further contended that the assessee was carrying on the business of purchase and sale of cloth in the years 1944 to 1947 and that the same business was carried on by the firm of which the assessee was a partner in the assessment year in question. As regards the submission made on behalf of the assessee to call for a supplementary statement of case, learned counsel for the department stated that no such statement was necessary as the question now sought to be raised was not raised before the Tribunal and, in any event, the compensation received by the assessee was not in respect of the business of dyeing cloth but in respect of the business of purchasing and selling cloth.

5. Now, it is well settled that in cases of claims for unliquidated damages, no debt is due until the amount is ascertained or admitted. In the instant case, the claim made by the assessee against the Nazarali Mills was in respect of unliquidated damages which were ascertained on 20th June, 1961, when the decree was passed in favour of the assessee. The right to receive the amount in question, therefore, accrued to the assessee on 20th June, 1961. In this connection, we may usefully refer to the following observations of the Supreme Court in *The Commissioner of Income Tax, Madras Vs. A. Gajapathy Naidu*, :

" In regard to the question, when and whether an income accrues or arises within the meaning of the first part of the said clause we have a decision of this court which has clearly enunciated the principles underlying the said expression : that is the decision in *E.D. Sassoon and Company Ltd. Vs. The Commissioner of Income Tax, Bombay City*, . In that decision, this court accepted the definition given to the words " accrue " and " arise " by Mukerji J. in *Rogers Pyatt Shellac Co. v. Secretary of State for India* [1925] 1 ITC 363, which is as follows:

" ...both the words are used in contradistinction to the word " receive " and indicate a right to receive. They represent a stage anterior to the point of time when the income becomes receivable and connote a character of the income which is more or less inchoate."

Under this definition accepted by this court, an income accrues or arises when the assessee acquires a right to receive the same. It is commonplace that there are two principal methods of accounting for the income, profits and gains of a business ; one is the cash basis and the other, the mercantile basis. The latter system of accountancy " brings into credit what is due immediately it becomes legally due and before it is actually received; and it brings into debit expenditure the amount for which a legal liability has been incurred before it is actually disbursed". The book profits are taken for the purpose of assessment of tax, though the credit amount is not realised or the debit amount is not actually disbursed. If an income accrues within a particular year, it is liable to be assessed in the succeeding year."

6. Now, it has been found that the assessee maintained its accounts on the mercantile basis. Therefore, the right to receive the income in question accrued to the assessee in the assessment year 1962-63, and the Tribunal was justified

in holding that the profit of Rs. 24,000 accrued to the assessee in the assessment year 1962-63.

7. It is now well settled that where damages are recovered for an injury inflicted on a man's trading, the amount of damages would be a trading receipt. Learned counsel for the assessee was unable to point out any reason for holding that, in the circumstances of the case, the Tribunal was not justified in holding that the amount of Rs. 24,000 received by the assessee was not in the nature of a capital receipt.

8. As regards the submission made on behalf of the assessee that the Tribunal be directed to send a supplementary statement of case giving its finding on the question as to whether the business of dyeing cloth was being carried on by the assessee during the assessment year 1962-63, we do not consider it necessary to give any such direction in the circumstances of this case. The only question urged before the Tribunal in this behalf was that the cloth business, in respect of which the amount of compensation was received by the assessee from Nazarali Mills, was not carried on by the assessee during the previous year relevant to the assessment year 1962-63. The Tribunal found that the business in cloth was carried on in the previous year by the firm of which the assessee was a partner. The question as to whether the compensation received by the assessee was for dyeing business and whether that business was carried on in the assessment year 1962-63 by the firm of which the assessee was a partner, was not raised before the Tribunal and was not, therefore, dealt with by the Tribunal. As the question now sought to be raised does not arise out of the order of the Tribunal, it is not necessary to call for a supplementary statement of case, as urged for on behalf of the assessee. In view of the findings that during the assessment year 1962-63 the assessee was a partner of the firm which carried on the business in cloth and that the claim made by the assessee against Nazarali Mills was for a compensation on account of the failure of Nazarali Mills to supply the bales of cloth to the assessee in connection with his cloth business during the period 1944 to 1947, the Tribunal was right in holding that the income of Rs. 24,000 was chargeable to tax u/s 28 of the Act.

9. For all these reasons, our answers to the three questions referred to us are in the affirmative and against the assessee. In the circumstances of the case, parties shall bear their own costs of this reference.