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Court : Andhra Pradesh

Decided On : Nov-15-1961

Reported in : [1962]45ITR464(AP)

Appeal No. : Case Referred No. 17 of 1960

Appellant : B.

Respondent : Hanumantha Rao V. Commissioner of Income-tax, Andhra Pradesh.

Judgement :

CHANDRA REDDY C.J. - The question to be answered by us in this reference under section 66(2) of the Indian Income-tax Act is :

'Whether, on the facts and in the circumstances of the case, the disallowance of the interest claimed by the petitioner is correct in law ?'

The relevant assessment year is 1953-54, the corresponding accounting year being the official year 1952-53. In the accounting year, the assessee claimed a sum of Rs. 4,631, as interest paid to the vendors of a baling press, he having purchased the press belonging to the Godavari Baling Society for Rs. 43,500 on credit, agreeing to pay interest at 12 per cent. in regard to the same. He did not pay interest either in the prior accounting year or in the present accounting year or in the present accounting year. Though he claimed the interest due for that year as an expenditure, since he did not pay the amount in question in the present

accounting year and did not make any adjustment of interest in the account of the baling press, as he had no accounts at all, the Income-tax Officer disallowed the interest claimed amounting to Rs. 4,631.

The appeal carried by the assessee to the Appellate Assistant Commissioner was allowed for the reason that, though the assessee had not maintained any books of account, he had prepared his returns and statements with the help of the duplicate bills and expense vouchers. It appears from the order of the Appellate Assistant Commissioner that the assessee, in accounting for the receipts in that way, had taken into account even the bills which had not been realised at the end of the accounting year as revenue receipts. He further observed :

'The interest has been allowed in the earlier year. The debtors had filed suits against the assessee and had obtained decrees for the full amount. I do not find any objection to the assessees method of computing the income by taking into account all the receipts and expenses on the accrual basis instead of the actual receipts or payments basis. The interest being definitely deductible from the income, I consider that the assessee should be allowed to deduct it from the income computed though there are no books and hence no entries crediting this interest to the respective persons. I do not also find any reason for departure from the earlier practice. This amount of Rs. 4,631 is allowed.'

What emerges from this order is that the assessee had been adopting the method of accounting by and under which he was bringing into credit amounts which fell due though not realised and bringing into debit sums of money which fell due though not actually paid, that the returns were being prepared by him with the help of duplicates of bills, that he had not maintained any regular accounts and that, lastly, the department treated such expenditure as allowable debits.

Dissatisfied with the conclusion of the Appellate Assistant Commissioner, the Income-tax Officer took the matter in appeal to the Tribunal. The Tribunal reversed the order of the Appellate Assistant Commissioner in the view that in a case where no accounts were kept, the system that should be deemed to have been adopted is 'cash' and, therefore, since no payment of interest was actually made by the assessee during the relevant year of account, he could not claim any allowance

thereof on the ground that liability for the payment had accrued during the year.

Thereupon, the assessee requested the Tribunal to make a reference under section 66(1) of the Income-tax Act. Since the Tribunal declined to do it, this court directed the Tribunal to state a case for the opinion of this court under section 66(2) on the question set out above.

In this references, Sri Anantha Babu, learned counsel for the assessee, impeaches the view of the Tribunal.

For solving the problem that presents itself before us, we have to look at section 13 in so far as it has a bearing on the present enquiry. It reads :

'Income, profits and gains shall be computed, for the purposes of section 10 and 12, in accordance with the method of accounting regularly employed by the assessee....'

It is clear from this section that the income of a person has to be determined with reference to this method of accounting employed by him. If the assessee adopts a particular method for the computation of the receipts and expenditure, that should form the basis of ascertainment of the income of an individual. There are two methods of accounting the income, profits and gains of a business, which are generally described as the 'mercantile basis' and 'cash basis'. The former consists in bringing into credit what is due, though not actually realised, and bringing into debit what is payable, though not paid actually, the other method being the ordinary one of taking into account only such sums as have been actually received and debiting such amounts as have been actually spent. Recognition has been given to the former method also by the Act as also by a long line of decisions.

It is enough for the purpose of this reference to advert to the judgment of the Supreme Court in Calcutta Co. Ltd. v. Commissioner of Income-tax. Observes Bhagwati J. who spoke for the court :

'The mercantile system of accounting is well-known and this method has been explained in a judgment of this court in Keshav Mills Ltd. v. Commissioner of Income-tax.'

His Lordship extracted the following passage from the cited case :

'That system brings into credit what is due, immediately it becomes legally due an 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.'

There can be little doubt that this is the method which has been employed by the assessee in the instant case. It is not disputed that he has shown as credits what was legally due notwithstanding this not having been actually received. A similar method he adopted with regard to expenditure also. Having elected to adopt a method of taxation in regard to expenditure. It may also be mentioned here that the department was treating this as a permissible deduction in the previous years. The fact that accounts were not maintained would not make material difference for the reason that it was with the aid of duplicates of bills that the returns were prepared both in regard to income and expenditure and this was accepted by the department in the prior years. It was the duplicates of bills that formed the basis of the returns in the preceding years. In our opinion, the view taken by the Assistant Commissioner is a sound one.

In disagreement with the Income-tax Appellate Tribunal, we answer the question in favour of the assessee and against the department. The assessee will get his costs from the department. Advocates fee Rs. 100 (one hundred).

Question answered accordingly.

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