

Jhalani and Co. Vs. Inspecting Assistant

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Court : Income Tax Appellate Tribunal ITAT Delhi

Decided On : Jan-12-1993

Reported in : (1993)45ITD67(Delhi)

Judge : J Kathuria, N Agarwal

Appellant : Jhalani and Co.

Respondent : inspecting Assistant

Judgement :

1. These are the two appeals relating to the assessment year 1985-86.

One by the assessee and the other by the revenue. Though both the appeals relate to different matters but since they pertain to the same assessee and same asst. year, it would be appropriate to dispose of both of them by a common order.

2. to 10. [These paras are not reproduced here as they involve minor issues.] 11. Appeal No. 357/DEL/1989 has been filed by the revenue on the following ground:- On the facts and circumstances of the case, the CIT (Appeals) has erred in law and on facts in deleting the addition of Rs. 13,25,662 on account of accrued commission.

The main Source of income of the assessee appears to be commission received from M/s. Gedore Tools India (P.) Ltd., which is now described as Jhalani Tools (India) Pvt. Ltd. The accounting period of the assessee is said to be July to June. The appellant had been disclosing income from commission on accrual basis and,

was, therefore, following the mercantile system of accounting. However, the assessee adopted cash system of accounting in the previous year relevant to the assessment year 1985-86. It was explained by the assessee that the reason for this change is the recurring loss being incurred by the principal, namely, Gedore Tools. It was contended that the appellant was facing difficulty in recovering the commission due to financial difficulties of its principal M/s. Gedore Tools. If the method of accounting is not changed the appellant would be required to bear taxes on the income which has not yet been received though it had become receivable. It was, therefore, argued that the change in method of accounting was bona fide.

12. The CIT (Appeals) has considered the contentions of the assessee and has agreed with them. He has found that there is no evidence of there being any connivance between the appellant and its principal M/s.

Jhalani Tools (Gedore Tools). It has also been held by the GIT (Appeals) that the change in the method of accounting is bona fide.

13. The learned DR has argued before us that looking to the entire facts of the case, the change in the method of accounting would not appear to be bona fide and it was only to avoid the payment of tax on the income by way of commission that a change of accounting system has been introduced. Reliance has been placed on State Bank of Travancore v. CTT [1986] 158 ITR 1021 wherein it was held that the concept of reality of income and the actuality of the situation are relevant factors which go to the making of accrual of income. It has been observed by the apex court that the concept of real income cannot be so used as to make accrued income non-income simply because after the event of accrual, the assessee neither decides to treat it as a bad debt nor claims deduction Under Section 36(2) of the Income-tax Act, 1961. In that case, the State Bank of Travancore showed certain amount of interest in a separate account called, the "Interest Suspense Account". This amount of interest was charged by the bank on advances which had become extremely doubtful of recovery and which the bank had termed "sticky advances". The amount of interest was debited in the accounts of the concerned parties but it was not carried to the Profit and Loss Account but

to the Interest Suspense Account. The bank claimed that having regard to the bad and deteriorating financial conditions of the parties concerned, the recovery of even the principal amounts of the debts had become improbable and doubtful and as such the interest therein, though debited to the respective debtors, was taken to the Interest Suspense Account to avoid showing inflated profits by including hypothetical and unreal income. It would be obvious that in the aforesaid case the bank had no intention to bring the income from interest to the P & L account and, therefore, the decision of the Supreme Court relates to such facts which are altogether different.

14. In the case before us, the assessee is only claiming that the amount may be taxed when it is received. It is with that intention that the assessee has changed over to the cash system of accounting. It has been urged that the change is bona fide and it is being consistently followed thereafter. Therefore, the change is not casual but has been consistently followed in subsequent years also.

15. The learned counsel for the assessee has relied upon CIT v. Rqjasthan Investment Co. (P.) Ltd. [1978] 113 ITR 294 (Cal.) wherein the question of change in the method of accounting was considered and it was held that if the change over is bona fide and is based on reasons, it cannot be disallowed. In Shiv Prasad Ram Sahai v. CIT [1966] 61 ITR 124 (All.) also the question of change in the system of accounting came to be examined and it was held that the choice is entirely that of the assessee and if he chooses to adopt a system of accounting and regularly employes that system, it is not open to change it thereafter.

16. The learned counsel for the assessee has also relied upon CIT v. West Coast Paper Mills Ltd. [1992] 193 ITR 349 (Bom.) wherein also the method of accounting was changed and it was held that if the method is followed regularly and is bona fide, there does not appear to be any reason why change should not be allowed.

17. It has been urged before us that the Delhi High Court has also in an Income-tax Reference No. 37 of 1972 decided on 9-11-1981 expressed the view that if there was a bona fide change in the method of accounting, the Deptt. must accept that change. In CIT v. Union Land and Building Society (P.) Ltd. [1972] 83 ITR 794 (Bom.) also the hybrid system of accounting in the year of change was permitted.

18. It has been contended on behalf of the assessee that the principal, namely, the Jhalani Tools have been incurring losses for the last 3-4 years. In the year 1981-82 there was a loss of Rs. 250 lakhs, in the accounting year 1982-83 (18 months), the loss amounted to Rs. 767 lakhs, and in the year 1984-85 loss was Rs. 301 lakhs. In subsequent years also, there have been staggering losses. It has been, therefore, argued that the payment of commission to the assessee has become doubtful because of the losses suffered by the principal. Though the turnover may not have declined but the losses have definitely been there and in view of the losses, the principals M/s. Jhalani Tools have been declared to be a sick unit by the Board for Industrial and Financial Reconstruction constituted by the Cent. Govt. Since M/s.

Jhalani Tools have been declared a sick unit in the year 1988, it is obvious that the financial condition of the principal is not good and, therefore, it has failed to discharge its financial obligations. It has failed to repay the institutional loss and has even defaulted in making contribution to the provident fund.

19. Looking to the entire facts and circumstances, we are of the view that the change over from the mercantile system of accounting by the assessee cannot be called to be other than bona fide. Since, the principal M/s. Jhalani Tools have become a sick unit due to heavy losses year after year, the assessee chose to change over from mercantile system to cash system of accounting. Unless there is lack of bona fides or there is a casual exercise of discretion for change over, it would not be appropriate to reject the change. In view of this, decision of the CIT(A) appears to be correct and no interference is called for.

20. In the result, the ITA No. 357/DEL/1989 filed by the revenue is dismissed.

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