HONBLE THE ACTING CHIEF JUSTICE RAMESH RANGANATHAN AND
THE HONBLE SRI JUSTICE GUDISEVA SHYAM PRASAD

REFERRED CASE NO.71 of 1993

01.05.2018

The Commissioner, Income-tax, Karnataka Central, Bangalore.. Applicant

The KCP Limited. . Respondent

!Counsel for Applicant: Sri J.V. Prasad, Learned Senior Standing Counsel for Income-tax
Counsel for respondent: Sri S. Ravi, Learned Senior Counsel for Sri Challa Gunarajnan,
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? Citations:

1) (1975) 98 ITR 189 (SC)
2) (1998) 231 ITR 849 (Bom)
3) (1971) 82 ITR 835 (SC)
4) (2013) 358 ITR 295(SC)
5) (2008) 298 ITR 373 (AP)
6) (1958) 33 ITR 681
7) (2008) 220 CTR (Del.) 404
8) [1975] 98 ITR 167 (SC)
9) (2000) 245 ITR 428 (SC)
10) (2015) 374 ITR 681 (T&AP)
11) (1971) 82 ITR 363 (SC)
12) (1964) 53 ITR 134 (SC)
13) (1997) 4 SCC 530
14) 1959 Supp (1) SCR 45 : AIR 1959 SC 82 : (1959) 35 ITR 298
15) (1986) 2 SCC 11
16) 53 I.T.R. 122
17) (1936) 4 ITR 71 (Pat. HC)
18) (1945) 13 ITR 224(All. HC)
19) (1996) 11 SCC 530
20) (1964) 7 SCR 767 : AIR 1964 SC 1653 : (1964) 53 ITR 114
21) (1967) 3 SCR 482 : AIR 1968 SC 114 : (1967) 66 ITR 378
22) AIR 1927 Mad. 841
23) (1996) 2 SCC 277
24) (2015) 7 SCC 540
25) 1991 Supp (2) SCC 618
26) [1954] 26 ITR 27 (SC)
27) (1963) 50 ITR. 495 (Mad)

28) AIR 1969 SC 501
29) 1953 SCR 950 : AIR 1953 SC 187 : (1953) 23 ITR 230
30) (1954) SCR 258
31) 1956 SCR 691 : AIR 1957 SC 49 : (1957) 31 ITR 28
32) (1905) 5 TC 159
33) (1965) 2 LLJ 175
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41) 1997 (3) ALD 540 = 1997 (3) ALT 492
42) (Judgment in W.A.No.403 of 2004 dated 26.11.2004)
43) (2009) 312 ITR 254X (SC)
44) MANU/DE/3570/2017
45) (1997) 227 ITR 172 (SC)
46) (1970) 77 ITR 857
47) (1906) 2 Ch.654 (Ch D)
48) AIR 1974 SC 1596
49) AIR 1989 SC 1933
50) 1993 (3) ALT 471 (F.B) = 1993 (6) SLR 1 (AP)
51) 1989 (3) SLR 713
52) 1993 (1) ALT 221 (DB)
53) AIR 1961 SC 398
54) [1943] 11 I.T.R. 328
55) (1978) 4 SCC 358
56) (1999) 8 SCC 338
57) (2012) 341 ITR 593
58) (2012) 208 Taxman 464 (Karn)
59) (1938) 6 ITR 36 = AIR 1938 PC 1
60) (2007) 13 SCC 673
61) (1921) 1 KB 64
62) 1945(2) ALL ER 499
63) 1948 (1) ALL ER 616
64) (Judgment in TRC No.153 of 2004 & Batch dated 05.10.2005)
65) AIR 1970 SC 1173 = (1969) 2 SCR 481
66) (1936) A.C. 1
67) (1869) 4 H.L. 100
68) AIR 1976 SC 1503 = (1976) 3 SCC 800
69) AIR 1957 SC 657 = 1957 SCR 837
70) 1901 AC 102
71) 1990 (2) SCC 231
72) (1999) 4 SCC 197
73) (1984) 19 TTJ 572 (All.)

74) (2017) 395 ITR 515
75) (1997) 7 SCC 655 = (1997) 228 ITR 71
76) (1995) 212 ITR 177 (Cal)
77) (1985) 1 SCC 345
78) (2004) 6 SCC 186
79) 1951 AC 737
80) (1970) 2 ALL.E.R 294
81) 1971 (1) WLR 1062
82) 1972 (2) WLR 537
83) AIR 1968 SC 647
84) 1901 AC 495
85) (1997) 5 SCC 289
86) (2008) 5 SCC 680
87) (1970) 2 SCC 192
88) (1989) 1 SCC 345

THE HONBLE THE ACTING CHIEF JUSTICE RAMESH RANGANATHAN AND THE HONBLE SRI JUSTICE GUDISEVA SHYAM PRASAD

REFERRED CASE NO.71 of 1993

JUDGMENT: {Per the Honble the Acting Chief Justice Ramesh Ranganathan}

The Income Tax Appellate Tribunal, Hyderabad bench, has referred the following questions for our opinion.

1. Whether, on the facts and in the circumstances of the case, the provision made for increase in wages on the basis of the Wage Board Award which became enforceable on the date of the publication of the award on 20.07.1983 could be accepted as a liability having accrued on 19.05.1983 within the previous year ended 30.06.1983, when the assessee agreed before the Arbitrators that the award shall come into operation from an earlier date?

2. Whether, on the facts and in the circumstances of the case, on a true construction of the agreements, the provision made for payment of commission by the assessee to the Sri Lankan agents was allowable as an accrued liability?

3. Whether, on the facts and in the circumstances of the case, the expenditure incurred under the agreements with the Sri Lankan agents will amount to an expenditure incurred for maintaining an agency abroad within the meaning of Section 35B(1)(b)(iv) of the Income Tax Act?

4. Whether, on the facts and in the circumstances of the case, the liability to pay the premium for insurance policy could be allowed as accrued liability within the previous

year ended 30.06.1983 even though the indemnity depended on payment of the premium which was made only subsequent to the end of the previous year?

5. Whether, on the facts and in the circumstances of the case, the liability to pay commission under the agreement dated 18.08.1981 with M/s. Annapurna Agencies accrued on the procurement of the purchase orders within the previous year ended 30.06.1983?

6. Whether, on the facts and in the circumstances of the case, the liability to pay the liquidated damages under the terms of the agreement accrued when the delivery was made within the previous year ended 30.06.1983?

QUESTION No.6:

In so far as question No.6 is concerned, the Tribunal, in its order in ITA No.834/Hyd/1989 dated 26.03.1991, followed its decision for the earlier assessment year 1982-1983 in the assessees own case, in I.T.A. No.1785 of 1986, and held that the right to receive the extra price arose when the delivery was made, and the assessee had actually accounted for the extra price when the goods were actually delivered. On finding that its order for the earlier year had led to a reference, which was pending in the High Court, Question No.6, as extracted hereinabove, was also referred to this Court.

This question, in so far as the assessees own case for the earlier assessment year 1982-83 is concerned, was considered in R.C.No.342 of 1991 and a Division bench of this Court, by its order dated 08.08.2013, answered the question in the affirmative, against the revenue and in favour of the assessee. Following the order of the Division bench, in R.C. No.342 of 1991 dated 08.08.2013, we answer question No.6 in the affirmative, against the revenue and in favour of the assessee.

QUESTION No.1:

For the assessment year 1984-85, the assessee filed its return on 30.06.1984 declaring a total income of Rs.1,47,92,909/-. A revised return was filed on 06.01.1987 declaring an income of Rs.1,71,92,147/-. The Income Tax Officer passed an assessment order on 05.01.1988 determining the total income of the assessee as Rs.11,95,39,861/-. Among the deductions claimed by the assessee, in its profit and loss account, was a provision for payment of increase in wages.

A joint reference was made to the arbitrators, in an industrial dispute between the cement manufacturers association and their workmen, on 04.12.1981. The parties filed a memo before the arbitrators on 19.05.1983 agreeing that the award of the arbitrators would come into effect from 01.01.1982, and continue to remain in force till 30.06.1986. Thereafter the Award was made on 11.07.1983 which was received by the Central Government on 14.07.1983, and was published in the Gazette of India dated 20.07.1983. In its accounts, for the accounting year 01.07.1982 to 30.06.1983, the assessee made a provision for expenses relating to increase in wages from 01.01.1982 to 30.06.1982 for

Rs.7,75,902/-, and for expenses relating to increase in wages from 01.07.1982 to 30.06.1983 for Rs.23,27,706/-, i.e for a total sum of Rs.31,03,608/-. The assessees claim, that these amounts should be deducted in computing their income, was rejected by the Income Tax Officer who opined that, since the Award itself was made after the end of the previous year, the assessee could not have worked out the provision for increase in wages; the Award became final only on its publication; and, since publication of the Award was beyond the previous year, the liability did not arise during the previous year. Accordingly, he disallowed the claim.

In appeal, the CIT (Appeals) agreed with the Income Tax Officer that the liability accrued only after the close of the relevant accounting period, and could not therefore be allowed as a deduction in the said year. In further appeal, the Tribunal held that, while the Award was no doubt made on 11.07.1983 after the end of the previous year on 30.06.1983, it was made before the accounts were closed on 29.09.1983; while an Award, under Section 17 of the Industrial Disputes Act, became enforceable on the date of its publication in the gazette, it came into operation, under Section 17(4) of the Industrial Disputes Act, with effect from the dates specified therein or on the date when the Award became enforceable; since the assessee had agreed, before the arbitrators on 19.05.1983, that the Award should come into operation from 01.01.1982, their liability to pay the increased wages accrued on 19.05.1983; and, as the liability was accepted, it could be taken into account in computing the income of the previous year which ended on 30.06.1983. As the question, which arose on these facts, was whether the liability had accrued on a date prior to the date when the award itself became enforceable, and since there was no decision on the retrospective effect of an award with reference to the creation of a liability, the Tribunal has referred this question for our opinion.

Sri J.V. Prasad, Learned Senior Standing Counsel for Income-tax, would submit that, in the case of an assessee following the mercantile system of accounting, the liability would arise or accrue only when the assessee becomes legally liable in respect of the same; till such time as the assessee is legally due, in respect of a liability, it cannot be said that the liability has accrued or has arisen to the assesee; in a situation where the liability may be contemplated, or the liability is uncertain on account of litigation or otherwise, such a liability can only be termed as a contingent liability, and not an accrued liability; it is only when a legally enforceable debt becomes due, can it be said that the liability has arisen, even if the amounts are actually paid at a later point of time; similarly, in the case of receipts, it is only when the assessee has acquired a legal right to receive the amounts, can receipt be said to have arisen to the assessee, even if they are not actually received; with respect to wages, liable to be paid on account of the Wage Board Award, the award was made only on 11.07.1983, it was received by the Central Government on 14.07.1983, and was published in the Gazette on 20.07.1983, i.e., all the three dates fall beyond the relevant previous year; the claim of the assessee, based on the Memo dated 19.05.1983, or on the retrospective date specified in the Gazettee, did not create any liability legally due by the assessee during the previous year relevant to the subject assessment year; the agreement between the parties was subject to an award being passed by the Wage Board; the submission of the learned Senior Counsel, appearing on behalf of the assessee, that, as the assessee was following the mercantile system of accounting, they were obligated to adhere to Accounting Standard 4, as per Section 145(2) of the Act and, on following the same, the amount is deductible, is not tenable; Section 145(2), as it now stands, was inserted for the first time w.e.f. 01.04.1997; the said provision was not in existence in so far as the relevant previous year is concerned; and, even otherwise, A.S. 4 does not aid the assessee in respect of the claim made under this head. Learned Senior Standing Counsel for Income-tax would rely on (1) Nonsuch Tea Estates Ltd. v. CIT, Madras ; (2) CIT v. Kirloskar Tractors Ltd. ; (3) Morvi Industries Ltd v. CIT (Cal) ; and (4) CIT v. Excel Industries Ltd. .

On the other hand Sri S. Ravi, Learned Senior Counsel appearing on behalf of the respondent-assessee, would submit that the increase in wages was agreed to, in principle, by both the Cement Manufacturers Association and the Workmen on 19.05.1983 by filing a Joint Memo before the Arbitrator; it is on the basis of the said memo that an award was passed on 11.07.1983, and the same was published in the Gazette dated 20.07.1983; therefore the liability, to pay the increased wages with effect from 01.01.1982, arose before the end of the previous year i.e., 30.06.1983, though the same was quantified, on the Award being passed, on 11.07.1983; the assessee, therefore, claimed Rs.31,03,608/- as deduction, as the said amount has been admitted as liability and became enforceable following the mercantile system of accounting; though this liability was quantified by the award dated 11.07.1983, as the accounts were finalized after the Award was published in the Gazette dated 20.07.1983, the assessee is entitled to claim deduction in terms of Accounting Standard (AS) 4, i.e Contingencies and Events Occurring After the Balance Sheet Date, issued by the Institute of Chartered Accountants of India (ICAI); the Accounting Standards (AS4 is relevant to the present case) issued by ICAI is a policy statement based on a number of Accounting Principles; if a business liability has definitely arisen in the accounting year, the deduction should be allowed although the liability may have to be quantified and discharged at a future date; the Accounting Standards were made mandatory only after the amendment to Sec.145 of the Income Tax Act, and Section 211 of Companies Act, 1956; though the Accounting Standards were not mandatory prior to the said amendments, the same was recognized to be a guiding principle to be adopted in Accounting Practice; judicial notice has been taken by this Court, in M.S. Raju v. Deputy Commissioner of Income Tax , regarding maintenance of accounts following AS- 4; the reason for amendment of Section 145, as explained by Circular No.717 dated 14.08.1995, was to standardize the Accounting system either on cash or mercantile system of accounting, but not mixed or Hybrid methods; and the said circular in (215 ITR (stat.) 70 @ pg. 103-104) reads thus:-

Methods of accounting and accounting standards for computing income:

44.1. Section 145(1) of the Income Tax Act prior to its amendment by the Finance Act, 1995, provided for computation of income from business or profession or income from other sources in accordance with the method of accounting regularly employed by the assessee. Income is generally computed by following one of the three methods of accounting, namely, (i) cash or receipts basis, (ii) accrual or mercantile basis, and (iii) mixed or hybrid method which has elements of both the aforesaid methods. It was noticed that many assesses are following the hybrid method in a manner that does not reflect the correct income. The Finance Act, 1995, has amended Section 145 of the Income-tax Act to provide that income chargeable under the head Profits and gains of business or profession or Income from other sources shall be computed only in accordance with either the cash or the mercantile system of accounting, regularly employed by an assessee. The first proviso to sub-section (1) of Section 145 has been deleted.

44.2. The Finance Act, 1995, has also empowered the Central Government to prescribe by notification in the Official Gazette, the accounting standards which an assessee will have to follow in computing his income under the head Profits and gains of business or profession or Income from other sources. These accounting standards wil be laid down in consultation with expert bodies like the Institute of Chartered Accountants.

44.3. The amendment will take effect from 1st April, 1997, and will, accordingly, apply in relation to the assessment year 1997-98 and subsequent years.

Sri S. Ravi, Learned Senior Counsel, would submit that the issue relates to whether allowability of increase in wages should be made in the Financial Year A.Y. 1984-85 or 1985-86, and there is no dispute on the allowability of the amount; in CIT v. Nagri Mills Co. Ltd the Bombay High Court, while dealing with a reference as to whether the Assessee was entitled for deduction towards bonus during the year 1952 or 1953, held that, by allowing such a deduction, there would be no consequence either in A.Y. 1952-53 or 1953-54; this view was followed by the Delhi High Court in CIT v. Shri Ram Pistons and Rings Ltd ; the Tribunal has rightly allowed the claim holding that Accounting Standard-4 permitted events, occurring after the Balance Sheet date and before finalization of Accounts, to be taken into account as the liability because of increase in wages accrued by virtue of the award dated 11.07.1983; and, once an amount is legally liable to be paid and enforceable though the same has not been actually incurred, such amount becomes expenditure and is allowable. Learned Senior Counsel would rely on Challapalli Sugars Ltd. v. CIT ; Bharat Earth Movers v. CIT ; CIT v. Pact Securities and Financial Services Ltd. ; M.S. Raju5; Nagri Mills Co. Ltd6; Shriram Pistons and Rings Ltd7; Kedarnath Jute Manufacturing Co. v. CIT ; Morvi Industries3 and CIT v. Swadeshi Cotton and Flour Mills).

In the present case, the assessment year is 1984-85, and the previous year relevant thereto is from 01.07.1982 to 30.06.1983. The assessee maintains its accounts on the mercantile system of accounting. The computation of income is to be made in accordance with the method of accounting regularly employed by the assessee. It may either be the cash system or it may be the mercantile system where entries are made on accrual basis, i.e., accrual of the right to receive payment and the accrual of the liability to disburse or pay. (Godhra Electricity Co. Ltd. v. CIT). Once the assessee has adopted the mercantile basis of accountancy, it is upon that basis, and that basis alone, that he has to be assessed. (Smt. Indermani Jatia v. CIT). There are two principal systems of book-keeping, firstly, the cash system in which a record is maintained of actual receipt and actual disbursements, entries being posted when money or money's worth is actually received, collected or disbursed. There is, secondly, the mercantile system, in which entries are posted in the books of accounts on the date of the transaction, i.e., on the date on which rights accrue or liabilities are incurred, irrespective of the date of receipt or payment. For example, when goods are sold on credit, a receipt entry is posted as on the date of sale, although no cash is received immediately in payment of such goods; and a debit entry is similarly posted when a liability is incurred although payment on account of such liability is not made at the time. (State Bank of Travancore v. CIT ; Commissioner of Income-Tax, Madras v. A. Krishnaswami Mudaliar).

According to the cash system, a record is kept of actual receipts and actual payments, entries being made only when money is actually collected or disbursed and, if the profits of the business are accounted for in this way, the tax is payable on the difference between the receipts and the disbursements for the period in question. In the mercantile system, under which a profit and loss account is maintained, the assets and liabilities are valued and entered in the accounts at the end of the financial year, and the difference between the two is the profit upon which the tax is paid. (Dhakeshwar Prasad Narain Singh v. Commissioner of Income Tax, Bihar & Orissa ; State Bank of Travancore15).

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. (Smt. Indermani Jatia14; Morvi Industries Ltd.3). The distinguishing feature of the mercantile system of accountancy is that it 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. (Commissioner of Income Tax v. Singari Bai ; State Bank of Travancore15). 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. (Smt. Indermani Jatia14; C.I.T v. Shiv Prakash Janak Raj & Co. Pvt Ltd.).

In the mercantile system of accountancy, the book profits are taken for the purpose of assessment of tax, though the credit amount is not realized or the debit amount is not actually disbursed. (CIT v. A. Gajapathy Naidu). Whenever the right to receive money, in the course of a trading transaction accrues or arises, even though income is not realised, income embedded in the receipt is deemed to arise or accrue. (Raja Mohan Raja Bahadur v. CIT). Where the assessee keeps the accounts according to the mercantile method of book-keeping, the effect of making a credit entry in the interest account would be to treat that amount as income or profits received by the assesses or treated by him as received for the purpose of tax. (CIT, Madras v. A.T.K.P.L.S.P., Subramaniam Chettiyar ; Smt. Indermani Jatia14).

An assessee, who follows the mercantile system of accounting, is entitled to deduct, from the profits and gains of the business, such liability which had accrued during the period for which the profits and gains were being computed, even though it is required to be discharged at a future date. (C.I.T v. Kalinga Tubes Ltd. ; Kedarnath Jute Manufacturing Co. Ltd.11). If a business liability has definitely arisen in the accounting year, the deduction should be allowed although the liability may have to be quantified and discharged later. What should be certain is the incurring of the liability. It should also be capable of being estimated with reasonable certainty, though the actual quantification may not be possible. If these requirements are satisfied the liability is not a contingent liability. It is a liability in praesenti, though it will be discharged at a future date. It does not make any difference if the future date, on which the liability has to be discharged, is not certain. (Taparia Tools Ltd. v. CIT ; Bharat Earth Movers9).

Where accounts are kept on accrual basis, profits or gains are credited though they are not actually realised. (Babulal Narottamdas v. CIT). Income can be held to accrue when the assessee acquires a right to receive that income. Income must be held to accrue on the date when a debt becomes due. (Babulal Narottamdas25; E.D. Sassoon & Co. Ltd. v. C.I.T.).

When the assesses is following the mercantile system of accounting, the liability to pay sales tax would accrue the moment the dealer made sales, which are subject to sales tax. At that stage the obligation to pay the tax arises. If the liability to pay the central sales tax arose or accrued, during the previous year relevant to the assessment year 1962-63, the liability to pay the quantified sales tax dues can be said to have accrued to the assessee for the relevant assessment year 1962-63, even though assessment, for that year, was completed by the Sales Tax Officer on 31.3.1966. If the tax liability is reduced in appeal/revision and if, in retrospect, it was found that, during the relevant assessment year, the assessee had claimed a large amount of deduction by way of business expenditure, the difference of the amount wrongly claimed and allowed in the earlier relevant assessment year can always be added back in the assessment of the relevant subsequent assessment year. (Kalinga Tubes Ltd.23; Kedarnath Jute Manufacturing Co. Ltd.11; Pope The King Match Factory v. Commissioner of Income-tax).

In Pope The King Match Factory27 a demand for excise duty was served-on the assessee who debited that amount in his accounts. on the last day of his accounting year and claimed the amount as a deductible allowance on the ground that he was keeping his accounts on the mercantile basis. The Madras High Court held that the assessee had incurred an enforceable legal liability on and from the date on which he received the Collector's demand for payment, and his endeavor to get out of that liability by preferring appeals did not detract from or retard the efficacy of the liability which had been imposed upon him by the competent excise authority. The law declared by the Madras High Court was approved by the Supreme Court in The Kedarnath Jute Mfg. Co. Ltd.11.

If a business liability has arisen in the accounting year, the deduction should be allowed even if such a liability may have to be quantified and discharged at a future date. (Bharat Earth Movers9; Taparia Tools Ltd.24). It is not open to the Income-tax Officer, if income has accrued to the assessee and is liable to be included in the total income of a particular year, to ignore the accrual, and thereafter tax it as income of another year on the basis of receipt. (Laxmipat Singhania v. C.I.T). If an assessee regularly adopts the mercantile system of accounting he would be liable to tax on the profits thus credited by him in his books of accounts subject to all permissible deductions. (Keshav Mills Ltd. v. CIT).

When an Income Tax Officer proceeds to include a particular income in the assessment, he should ask himself, inter alia, two questions, namely, (i) what is the system of accountancy adopted by the assessee? and (ii) if it is the mercantile system of accountancy, subject to the deemed provisions, when has the right to receive that amount accrued? If he comes to the conclusion that such a right accrued or arose to the assessee in a particular accounting year, he should include the said income in the assessment of the succeeding assessment year. No power is conferred on the Income Tax Officer under the Income-tax Act, to relate back an income, that accrued or arose in a subsequent year, to another earlier year on the ground that the said income arose out of an earlier transaction. (A. Gajapathy Naidu20).

As the assessee, in the present case, is maintaining its books of accounts on the mercantile system of accounting, the question which necessitates examination is when its liability, to pay increased wages to its workmen, arose. In order to answer this question, it is necessary to take note of the relevant statutory provisions. In an industrial dispute between the Cement Manufacturers Association and their Workmen, a joint reference was made for arbitration under Section 10-A of the Industrial Disputes Act on 04.12.1981. Section 2(b) of the Industrial Disputes Act, 1947 defines an award to mean an interim or a final determination of any industrial dispute, or of any question relating thereto, by any Labour Court, Tribunal or National Industrial Tribunal and includes an arbitration award made under Section 10-A. Section 10-A relates to voluntary reference of disputes to arbitration and, under sub-section (1) thereof, where any industrial dispute exists or is apprehended, and the employer and the workmen agree to refer the dispute to arbitration, they may, at any time before the dispute has been referred under Section 10 to a Labour Court or Tribunal or National Tribunal, by a written agreement, refer the dispute to arbitration and the reference shall be to such person or persons (including the presiding officer of a Labour Court or Tribunal or National Tribunal) as an arbitrator or arbitrators as may be specified in the arbitration agreement. Section 10-A(3) requires a copy of the arbitration agreement to be forwarded to the appropriate Government and the Conciliation Officer, and the appropriate Government shall, within one month from the date of receipt of such a copy, publish the same in the official gazette. Under Section 10-A(3A) where an industrial dispute has been referred to arbitration and the appropriate Government is satisfied that the persons making the reference represent the majority of each party, the appropriate Government may, within the time referred to in sub-section (3), issue a notification in such manner as may be prescribed; and when any such notification is issued, the employers and workmen who are not parties to the arbitration agreement but are concerned in the dispute, shall be given an opportunity of presenting their case before the arbitrator or arbitrators. Section 10-A(5) stipulates that nothing in the Arbitration Act, 1940 shall apply to arbitration under Section 10-A.

The parties to the industrial dispute i.e. the Cement Manufacturers Association and their Workmen filed a memo before the arbitrators on 19.05.1983 agreeing that the arbitrators award may be given effect to from 01.01.1982, and to continue to remain in force till 30.06.1986. The award was passed by the arbitrators only 11.07.1983 which is beyond the previous year 01.07.1982 to 30.06.1983. This award dated 11.07.1983 is said to have been received by the Government of India on 14.07.1983 and was, admittedly, published in the Gazette of India on 20.07.1983.

The question which necessitates examination is when the liability to make payment, in terms of the arbitration award dated 11.07.1983, accrued. The assessee made a provision for expenses relating to increase in wages from 01.01.1982 to 30.06.1982 for Rs.7,75,902/-, and for expenses relating to increase in wages from 01.07.1982 to 30.06.1983 for Rs.23,27,706/- i.e for a total sum of Rs.31,03,608/- in its books of accounts for the previous year 01.07.1982 to 30.06.1983. The manner in which the assessee recorded its liability in its books of accounts is not conclusive, for the test to be applied, in cases where an assessee is regularly maintaining its books of accounts on the mercantile system of accounting, is when the liability accrued, and it is only on the date of accrual of such expenditure can the assessee claim its deduction from their income during the relevant previous years. The liability to pay tax on the income arises when it has arisen or accrued, and how the assessee deals with it subsequently does not affect that liability. (CIT v. K.R.M.T.T. Thyagaraja Chetty ; Sree Meenakshi Mills Ltd. v. CIT). Whether income tax is due or not cannot be determined according to the manner in which the person, making the profit, pleases to deal with it. (Californian Copper Syndicate (Limited and Reduced) v. Harris (Surveyor of Taxes ; Raja Mohan Raja Bahadur21). A party cannot avoid tax by adopting the simple expedient of not disclosing its receipt in his books. That will be a case of income accrued or arisen but concealed and not of income not accrued or arisen. (Sree Meenakshi Mills Ltd.31).

The liability, regarding increase in wages, arose only in terms of the arbitration award made under Section 10-A of the Industrial Disputes Act. Section 17 of the Industrial Disputes Act, as it then stood, relates to publication of reports and awards and, under sub-section (1) thereof, every arbitration award shall, within a period of thirty days from the date of its receipt by the appropriate Government, be published in such manner as the appropriate Government thinks fit. Section 17(2) stipulated that, subject to the provisions of Section 17-A, the award, published under sub-section (1), shall be final and shall not be called in question by any Court in any manner whatsoever. Section 17-A related to commencement of the award and, under sub-section (1) thereof, an award (including an arbitration award) shall become enforceable on the expiry of thirty days from the date of its publication under Section 17.

Though the proviso to Section 17-A(1) does not appear to have any application to arbitration awards, it is nonetheless necessary to note its contents as reliance is placed, on behalf of the assessee, on a judgment of this Court whereby the proviso was declared ultravires the constitutional scheme. Under proviso (a) to Section 17-A(1), if the appropriate Government is of opinion, in any case where the award has been given by a Labour Court or Tribunal in relation to an industrial dispute to which it is a party, that it will be inexpedient on public grounds affecting national economy or social justice to give effect to the whole or any part of the award, the appropriate Government, or as the case may be, the Central Government may, by notification, in the official gazette, declare that the award shall not become enforceable on the expiry of the said period of thirty days.

While Section 17(1) required an arbitration award to be published, and on its publication to attain finality under Section 17(2), Section 10-A(3) requires the appropriate Government, within one month from the date of receipt of a copy of the award, to publish the same in the official gazette. Section 17-A(1), as it then stood, stipulated that, after expiry of the 30 days period from the date of its publication under Section 17, the award shall become enforceable.

Ordinarily, an award comes into operation from the time stated in Section 17(1) or Section 10-A(3) of the I.D. Act i.e., on its publication in the Gazette. The Tribunal, however, is given the power to order that its award shall be applicable from another date (All India Reserve Bank Employees Association v. Reserve Bank of India), even from a date prior thereto. Retrospective operation implies the operation of the award from a date prior to the reference, and the word 'retrospective' cannot apply to the period between the date of the reference and the award. (Wenger & Co. v. Their Workmen ; All India Reserve Bank Employees Association33).

Section 17(4) gives a discretion to the Tribunal, and no general principle is either possible or desirable to be stated in relation to the fixation of the date from which the award should operate. (All India Reserve Bank Employees Association; The Hindustan Times Ltd. v. Their Workmen). A discretion "exercised on judicial principles by the Tribunal, about the commencement of the award, should, ordinarily, not be interfered with. (All India Reserve Bank Employees Association v. Reserve Bank of India33; Remington Rand of India v. Workmen ; Rajkamal Kalamandir (P) v. Indian Motion Picture Employees Union ; and Western India Match Company Ltd. v. Their Workmen).

As the award itself was made only on 11.07.1983, after the end of the previous year 01.07.1982 to 30.06.1983 for the relevant assessment year 1984-85, the liability to pay increased wages, in terms of the arbitration award dated 11.07.1983, can be said to have accrued only thereafter, and not prior thereto in the previous year 01.07.1982 to 30.06.1983. The mere fact that a joint memo was filed by the Cement Manufacturers Association and its members before the arbitrator on 19.05.1983 agreeing that the award be made applicable from 01.01.1982 is of no consequence, as it is only on an award being passed, could the joint memo be given effect to. Consequently, the assessee was not entitled to claim deduction of these amounts in the previous year relevant to the Assessment year 1984-85, merely because a joint memo was filed before the arbitrator on 19.05.1983, as their liability, to make payment of the increased wages, accrued only in terms of the arbitration award made on 11.07.1983, after the end of the previous year 01.07.1982 to 30.06.1983.

As noted hereinabove, the arbitrators award was published in the Gazette of India, as required under Section 10-A(3) of the Industrial Disputes Act, on 20.07.1983. That the parties to the Award, i.e., the Cement Manufacturers Association and their Workmen, had agreed before the arbitrators on 19.05.1983, only means that, in terms of the said joint memo, the award would apply from an anterior date i.e., from 01.01.1982. The distinction, between the date from which the award is enforceable and the date from which it comes into operation, must be borne in mind. Although, normally, the date of enforceability and the date of operation may be identical, yet there may be cases where these two dates may be different. The date from when the award of a Tribunal shall be operative is the date specifically mentioned as such in the award itself. The date of enforceability of the award of a Tribunal is the date which comes on the expiry of 30 days from the date of its publication under Section 17. A simple illustration will make this point clear. If an award specifically mentions that it is to come into operation on 10.11.1950, then that date is the date from which the award becomes operative. If the award is published in the Gazette on 15-11-1950, it will be enforceable, 30 days after its publication, on 16-12-1950. The enforceable date in this case is not the same as the date of operation of the award. The two dates are different. The directives given in the award, though operative, will not be enforceable except from 16-12-1950, and when it becomes enforceable then all the directions in the award must be implemented from the date of its operation, viz. 10-11-1950. If, however, it is not specifically mentioned in the award as to the date from which the award shall come into operation, then the date of operation as well as the enforceable date will be identical, that is to say, the date which falls on the expiry of 30 days from the date of its publication under Section 17. (South Travancore Electrical Workers Union v. Nagercoil Electric Supply Corporation).

Under the provisos to Section 17A(1) of the Industrial Disputes Act, before the expiry of 30 days, the appropriate Government has been given the power to declare in certain cases that the award shall not become enforceable on the expiry of the said period of 30 days. This declaration should be made before the expiry of 30 days. In other words, the enforceability of the award may be postponed beyond thirty days under certain circumstances by the appropriate Government. No award is, therefore, enforceable before the expiry of 30 days and, therefore, no obligation is to be discharged before the expiry of the said period. There is no obligation on the employer to implement the award before expiry of 30 days from its publication. (The State of Maharashtra v. Ajit Maneklal Choksi).

Under Section 17-A(1) of the Industrial Disputes Act, an award shall become enforceable 30 days after its publication in the official gazette and since the Award, in the present case, was published in the Gazette of India on 20.07.1983, it was enforceable 30 days thereafter on and from 19.08.1983 onwards. While the award became enforceable only on 19.08.1983, payment under the award was required to be made with retrospective effect from 01.01.1982. The liability to make payment in terms of the award accrued only on the date on which the award became enforceable, and the fact that, on the date on which it is enforceable, the payment, in terms of the award, is required to be made retrospectively from 01.01.1982 does not result in accrual of liability from a retrospective date i.e., 01.01.1982, as the liability to make payment arose only under the Award passed on 11.07.1983, published in the Gazette of India on 20.07.1983, and which was enforceable on and from 19.08.1983 onwards; and all these three dates are beyond the relevant previous year 01.07.1982 to 30.06.1983.

In Telugunadu Workcharged Employees State Federation v. Govt. of India , the question whether the provision, contained in the proviso to Section 17-A (1) of the Act, was offensive of the Constitutional Scheme or any of the Constitutional provisions arose for consideration. A Learned Single Judge of this Court observed:

..But, the impugned provision, in the instant case, makes a distinction with regard to enforcement of the awards and while the awards rendered inter-se the workmen and the private sector undertakings are made binding and compulsorily enforceable, reserves the power to the Government to annul the award on the ground of either national economy or public interest, if the Government is a party to the dispute and suffered the award. This is clearly violative of equality clause guaranteed under Article 14 of the Constitution of India and the impugned provision is unconstitutional on this ground.

The Constitution has assigned the Courts the function of determining as to whether the laws made by the legislature are in conformity with the provisions of the Constitution. In adjudicating the constitutional validity of the statutes, the Courts discharge an obligation which has been imposed on them by the Constitution. The Courts would be shirking their responsibility if they hesitate to declare the provisions of a statute to be unconstitutional, even though those provisions are found to be violative of constitutional scheme or the provisions. In view of what is stated supra and as I have come to the clear and unmistaken conclusion that the impugned provision encroaches upon the judicial power of the State, as it violates the basic concept of rule of law and democratic pattern envisaged by the Indian Constitution, unhesitatingly, I strike down the impugned provision as being ultra vires the Constitution and consequently the provision contained under Section 17(2) of the Act to the extent of the words "subject to the provisions of Section 17-A" and whole of Section 17-A with sub-sections 1 to 4 thereof are non est under law. As an inevitable corollary, G.O.Ms. No. 2, Labour Department, dated 20-1-1994 is quashed as being unsustainable in view of what is held above. Now, the award which has been published in G.O.Rt. No. 2761, Women's Development, Chief Welfare and Labour Deparment, dated 23- 12-1993 shall be operative and the same be implemented by respondents 3 to 5 within a period of one month from the date of receipt of a copy of this order.. (emphasis supplied) Since Section 17-A of the Industrial Disputes Act, 1947 has been held ultra vires the Constitution, in Telugunadu Workeharged Employees State Federation41, which is a binding precedent, the Government has no power to issue an order nullifying an award, and declaring it as not enforceable on public grounds. (Govt. of A.P v. Nagarjunasagar Dam Employees & Labour Union rep. by its Secretary).

While it is no doubt true that a Learned Single Judge of this Court had declared Section 17-A, and a part of Section 17(2), ultra-vires the Constitution of India, the order in Telugunadu Workcharged Employees State Federation was passed on 23.04.1997, more than 13 years after the end of the subject previous year i.e. 30.06.1983. Even if the said judgment is held to apply to the present case, and Sections 17 and 17-A are held inapplicable, even then the award itself was made on 11.07.1983, and was published, as required under Section 10-A(3) of the Industrial Disputes Act, in the Gazette of India on 20.07.1983, both of which are beyond the end of the previous year 01.07.1982 to 30.06.1983; and, since the liability to pay increased wages accrued under the award, the liability of the assessee to make payment of increased wages can be said to have accrued only on or after 11.07.1983 when the award was made, and was published in the official Gazette, and not prior thereto.

In Nonsuch Tea Estates Ltd.1, the question which arose for consideration was whether the Managing Agency remuneration, for the period 01.04.1956 to 30.06.1957, was deductible in computation of the income of the previous year ending 30th June 1958, relevant for the assessment year 1959-60. By an agreement entered into between the appellant and the managing agents, the latter were reappointed for a period of 10 years on a remuneration of 5% commission on the net profits of the company computed in the manner laid down in Sections 349 to 351 of the Companies Act, 1956. The revised terms were to take effect from 01.04.1956. As required by Section 326 of the Companies Act, the new agreement was sent to the Central Government for approval on 03.08.1957. The Government conveyed its approval on 02.09.1957 for appointing managing agents with effect from 01.04.1956. The appellant followed the mercantile system of accounting, and credited a sum of Rs.9,320/- to the account of the managing agents, as their remuneration, during the period 01.07.1955 to 30.06.1956. For the purpose of income-tax, the Company added back the said sum of Rs.9,320/- to its taxable income. It followed the same procedure for the year ending 30.06.1957, relevant to the assessment year 1958-59. However for the assessment year 1959-60, for which the previous year was 01.07.1957 to 30.06.1958, the assessee showed the managing agents remuneration, payable during that year, as Rs.97,188/-. Though this amount did not pertain to the previous year, relevant to the assessment year 1959-60, the Company claimed it as deductible expenditure for that year on the ground that the sum became payable only during that year when the Government accorded its approval to the new agreement. The Income-tax Officer rejected this claim holding that the approval of the Central Government was necessary only for actual payment, the assessee should have ascertained the liability for each year, and claimed it on the mercantile basis which was the system adopted by them. It is in this context that the Supreme Court observed:

.In our judgment the High Court was in error in answering the question referred to it against the assessee. It appears that the Income-tax authorities, the Tribunal and the High Court all laid special emphasis on the fact that the Company followed the mercantile system of accounting. The distinction between the two methods of accounting, one on the cash basis and the other on the mercantile basis is well-known. In Commissioner of Income-tax, Madras v. A. Gajapathy Naidu : 1964) 53 I.T.R. 114 (SC), this Court explained the difference betwe in the two methods quoting with approval an extract from a Judgment of the, Allahabad High Court in Commissioner of Income-tax v. Singari Bai : (1945)13 I.T.R. 224). In Gajapathy Naidu's case this Court said: " 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.

However, even an assessee following the mercantile system of accounting is not entitled to claim a deduction until liability for the sum for which deduction is claimed has accrued. The reasons given by the High Court overlook the plain terms of Section 326 of the Companies Act, 1956. Section 326 so far it is material for the question involved in this case, is in these terms :

> "Sec. 326.(1) In respect of any company............
> (a)..........

(b) unless the approval of the Central Government has been obtained for such appointment or re-appointment.

(2) The Central Government shall not accord its approval under sub- section (1) in any case, unless it is satisfied (a) that it is not against the public interest to allow the company to have a managing agent; (b) that the managing agent proposed is, in the opinion, a fit and proper person to be appointed or re-appointed as such, and that the conditions of the managing agency agreement proposed are fair and reasonable; and (c) that the managing agent proposed has fulfilled any conditions which the Central Government requires him to fulfil."

Section 326 prohibits the appointment or re-appointment of a managing agent unless the Central Government approved such appointment or re- appointment. The Central Government would not accord its approval unless the requirements specified in clauses (a), (b) and (c) of sub-section (2) of the section have been fulfilled. Therefore, it cannot be assumed that the Central Government will approve every proposed appointment or reappointment of a managing agent. Thus in the instant case it is only when the Central Government conveyed its approval to the appointment of M/s. Harrisons and Crosfield Limited as managing agents by its letter dated September 2, 1957 that the appointment became effective and the Company's liability to pay the remuneration of the managing agents accrued. The position here is not that the liability had arisen earlier and its quantification only depended on the approval of the Central Government. It is true that the liability became effective from April 1, 1956, a date anterior to the relevant previous year, but 'that is because the Central Government chose to give its approval retrospective operation. The liability in these circumstances cannot be said to have arisen from any date prior to September, 2, 1957 when the approval was given as Section 326 contains an absolute prohibition against the appointment or re-appointment of a managing agent before the approval of the Central Government was obtained. In our opinion, the position is quite clear from the terms of Section 326 and we do not consider it necessary to refer to the authorities cited by the learned counsel for either side. (emphasis supplied) The law declared by the Supreme Court, in Naonsuch Tea Estates Ltd.1, is that, in view of Section 326 of the Companies Act, the liability of the appellant, to pay the remuneration of the Managing agents, accrued only when the Central Government conveyed its approval to the appointment of the Managing agents, and the mere fact that the Central Government gave its approval retrospective operation, did not result in the liability arising from any date anterior to the date on which approval was granted by it. Likewise, in the present case, the liability to pay increased wages arose, in view of Section 17(1) read with Section 10-A(3) of the Industrial Disputes Act, after the award was published in the Gazette, and the mere fact that the award required increased wages to be paid from a retrospective date i.e 01.01.1982 did not result in accrual of liability, prior to the date of the award i.e 11.07.1983 or from the date of publication of the award in the Gazette on 20.07.1983.

In Swadeshi Cotton and Flour Mills Pvt Ltd.12, the assessee had paid a sum, by way of profit bonus, to its employees in the calendar year 1947 in terms of the award made on 13.01.1949 under the Industrial Disputes Act. It debited this amount to its profit and loss account for the year 1948. The books for the year 1948 had not been closed till the date of the award of the Industrial Tribunal i.e 13.01.1949. The bonus was paid to the employees in the calendar year 1949, relevant to the assessment year 1950-51. The assessee was following the mercantile system of accounting. It is in this factual matrix that the Supreme Court observed:

.It follows from the above decisions of this Court that:-

(a) workmen are entitled to make a claim to profit bonus if certain conditions are satisfied;

(b) the workmen have to make a claim from year to year;

(c) this claim has either to be settled amicably or by industrial adjudication; and

(d) if there is a loss or if no claim is made, no bonus will be permissible.

In our opinion it is only when the claim to profit bonus, if made, is settled amicably or by industrial adjudication that a liability is incurred by the employer, who follows the mercantile system of accounting, within Section 10(2)(x) read with Section 10(5) of the Act.

On the facts of this case, it is clear that it was only in 1949 that the claim to profit bonus was settled by an award of the Industrial Tribunal. Therefore, the only year the liability can be properly attributed to is 1949, and hence we are of the opinion that the High Court was right in answering the question in favour of the assessee (emphasis supplied).

The law declared, in Swadeshi Cotton and Flour Mills Pvt. Ltd12, is that it is only when the claim is settled by industrial adjudication (in the present case the arbitral award passed under the Industrial Disputes Act) that a liability is incurred by the employer-assessee. As, in the present case, the Award itself was passed only on 11.07.1983, the liability was incurred by the assessee only on that date or thereafter when it was published in the Gazette on 20.07.1983 or from the date of its enforcement under Section 17-A(1) of the Industrial Disputes Act on 19.08.1983. As the award itself was passed on

11.07.1983, the liability to pay increased wages arose only in the previous year 01.07.1983 to 30.06.1984, and the assessee was not entitled to claim deduction towards this liability in the previous year 01.07.1982 to 30.06.1983.

It is, however, contended on behalf of the assessee, that even events beyond the balance sheet date must be taken into consideration in view of Accounting Standard-4 issued by the Institute of Chartered Accountants of India. Accounting Standard (AS) 4 relates to contingencies and events occurring after the balance sheet date. This standard deals with the treatment in financial statements of (a) contingencies and (b) events occurring after the balance sheet date. Clause 3.2 of (AS) 4 defines events, occurring after the balance sheet date, to be those significant events, both favourable and unfavourable, that occur between the balance sheet date, and the date on which the financial statements were approved by the Board of Directors in the case of a company. Two types of events can be identified (a) those which provide further evidence of conditions that existed at the balance sheet date; and (b) those which are indicative of conditions that arose subsequent to the balance sheet date. Accounting Standard-4, which relates to contingencies and events occurring after the balance-sheet date, cannot be applied to determine the liability to tax under the Income-tax Act. The question which necessitates examination is whether the liability, which accrued on the award being passed on 11.07.1983 and its being published in the Gazette on 20.07.1983, can be treated as a liability which accrued in the previous year 01.07.1982 to 30.06.1983, which, in its entirety, is a period prior thereto.

In CIT v. Woodward Governor India P Ltd. the Supreme Court, having come to the conclusion that valuation was a part of the accounting system, business losses were deductible under Section 37(1) on the basis of ordinary principles of commercial accounting, and the Central Government had made Accounting Standard-11 mandatory, examined the said Accounting Standard ("AS").

In The Chamber of Tax Consultants v. Union of India it was held that, if the power to notify standards had to be exercised consistent with the recognised ASs that did not contradict any principle recognised in the Act or as explained in judicial precedents, it would be a permissible exercise of the delegated power of notifying ASs; however, where the notified AS or, as in this case, the ICDS seeks to alter the system of accounting, or according accounting or taxing treatment to a particular transaction, then it will require the legislature to step in to amend the Act to incorporate such change; this may be unique to a fiscal statute like the Act; however, in the guise of a delegated power, the Central Government could not do what was otherwise legally impermissible.

In M.S. Raju5, a Division bench of this Court observed: .The Accounting Standards relied on behalf of the assessee are those prescribed by the Institute of Chartered Accountants of India. Thereunder, the definition "events occurring after the balance-sheet date" are those significant events, both favourable and unfavourable, that occur between the balance-sheet date and the date on which the financial statements are approved by the board of directors in the case of a company and by the corresponding approving authority in the case of any other entity. Under paragraph 8.1, events, which occur between the balance- sheet date and the date on which the financial statements are approved, may indicate the need for adjustments to assets and liabilities as at the balance-sheet date or may require disclosure. Under paragraph 8.2, adjustment to assets and liabilities are required for events occurring after the balance-sheet date that provide additional information materially affecting the determination of the amounts relating to conditions existing at the balance-sheet date.

As has been contended before the Tribunal, on behalf of the Revenue, even the audit report does not contain any note mentioning the specific facts as claimed by the assessee. There is nothing on record before us to indicate that the auditors had followed Accounting Standard No. 4. In such circumstances it is wholly unnecessary for us to examine whether Accounting Standard No. 4 would have required the assessing authority to take note of events which took place after the end of the assessment year in question.. (emphasis supplied) In Challapalli Sugars Ltd.8, on which reliance is placed on behalf of the assessee, the Supreme Court observed that the expression actual cost had not been defined, and it should be construed in the sense which no commercial man would misunderstand; and, for this purpose, it would be necessary to ascertain the connotation of the expression in accordance with the normal rules of accountancy prevailing in commerce and industry. Reference was made by the Supreme Court to Accountancy by Pickles, 1955, Spicer & Peglars Practical Auditing, Higher Book-keeping & Accounts by Cropper Morris & Fison, on Section 208 of the Companies Act, 1956 and on para 2.5 and para 2.2 of the statement of Auditing Practices issued by the Institute of Chartered Accountants of India. Thereafter the Supreme Court observed that the accepted accountancy rule, for determining the cost of the fixed assets, was to include all expenditure necessary to bring such assets into existence, and to put them in a working condition; in case money was borrowed by a newly started company, which was in the process of constructing and erecting its plant, the interest incurred before the commencement of production, on such borrowed money, could be capitalised, and added to the cost of the fixed assets which had been created as a result of such expenditure.

It is in this context that the Supreme Court, in Challapalli Sugars Ltd.8, observed that the above rule of accountancy should, in their view, be adopted for determining the actual cost of the assets, in the absence of any statutory definition or other indication to the contrary. Thereafter, relying on Section 208(1)(b) of the Companies Act, the Supreme Court held that this provision gave a statutory recognition to the principle of capitalising the interest in case interest is paid on money raised to defray expenses of the construction of any work or building, or the provision of any plant, in the contingencies mentioned in that Section, even though such money constituted share capital. The Supreme Court, thereafter, observed that the same principle should hold good if interest is paid on money not raised by way of share capital, but taken on loan for the purpose of defraying the expenses of the construction of any work or building or the provision of any plant.

The law declared by the Supreme Court, in Challapalli Sugars Ltd.8, is not that the accounting standards framed by the Institute of Chartered Accountants of India would automatically apply but is that, in the absence of any statutory definition or other indication to the contrary, the accepted rules of accountancy should be adopted for determining the actual cost of the asset. No such question arises for consideration in the case on hand.

In Tuticorin Alkali Chemicals and Fertilizers Ltd. v. Commissioner of Income-tax , the assessee had approached the Supreme Court against the order of the Madras High Court. In its order, the Madras High Court had held that the Institute of Chartered Accountants of India was a recognised authority on accounting principles; this fact was recognised by the Supreme Court in Challapalli Sugars Ltd.8; and, therefore, its view had to be respected. It is in this context that a three judge bench of the Supreme Court, in Tuticorin Alkali Chemicals and Fertilizers Ltd.45, observed that it was true that the Supreme Court had very often referred to accounting practices for ascertainment of profit made by a company, or the value of the assets of a company; but when the question was whether a receipt of money was taxable or not, or whether certain deductions from that receipt was permissible in law or not, the question had to be decided according to the principles of law, and not in accordance with accountancy practice; accounting practice cannot override the provision of the Income Tax Act; and, as was pointed out by Lord Russell in B.S.C. Footwear Ltd. v. Ridgway (Inspector of Taxes) , the Income Tax law does not march step by step in the footprints of the accountancy profession.

The Supreme Court, in Tuticorin Alkali Chemicals and Fertilizers Ltd45, further held that the question, in Challapalli Sugar Ltd.8, was about computation of depreciation and development rebate under the Indian Income Tax Act; in order to calculate depreciation and development rebate it was necessary to find out the actual cost of the plant and machinery purchased by the company; the Supreme Court had held that cost was a word of wider connotation than price, and there was a difference between the price of a machinery and its cost; Supreme Court had, thereafter, pointed out that the expression "actual cost" had not been defined in the Act; it was, therefore, necessary to find out the commercial sense of the phrase; as the expression "actual cost" had not been defined, it should be construed in the sense which no commercial man would misunderstand; for this purpose it would be necessary to ascertain the connotation of the above expression in accordance with the normal rules of accountancy prevailing in commerce and industry; and the accepted accountancy rule, for determining cost of fixed assets, was to include all expenditure necessary to bring such assets into existence and to put them in working condition; the Supreme Court had also taken note of Section 208(10(b) of the Companies Act, and had observed that the said provision gave statutory recognition to the principle of capitalising interest, in case the interest is paid on money raised to defray expenses of the construction of any work or building or the provision of any plant in contingencies mentioned in that Section, even though such money constituted share capital; the Supreme Court had also relied on an English case in Hinds v. Buenos Ayres Grand National Tramways Co. Ltd. ; wherein it was held that the cost of construction will be the amount actually spent, and also the interest payable on the amount borrowed during the period of construction; the judgment in Challapalli Sugars Ltd.8 showed that the Court was not in any way departing from legal principles because of any opinion expressed by the Institute of Chartered Accountants; the phrase actual cost was not defined in the Act, and therefore it had to be understood in commercial parlance; to find that out, the normal rule of accountancy prevalent in commercial and industrial circles was noted; the

Supreme Court, however, did not stop there and had pointed out that the principle of capitalising interest was to be found in Section 208 of the Companies Act itself and was also consistent with the views of the English Courts.

Thereafter the Supreme Court, in Tuticorin Alkali Chemicals and Fertilizers Ltd.45 held that, the question whether a particular receipt was of the nature of income, and fell within the charge of Section 4 of the Income Tax Act, was a question of law which had to be decided by the Court on the basis of the provisions of the Act, and the interpretation of the term income given in a large number of decisions of the High Courts, the Privy Council and also the Supreme Court; and it was well-settled that income attracted tax as soon as it accrued.

While the judgment in Challapalli Sugars Ltd.8 is that of a two Judge bench of the Supreme Court, the judgment in Tutirorin Alkali Chemicals and Fertilizers Ltd.45 is that of a three Judge bench of the Supreme Court. As the judgment in Challapalli Sugars Ltd.8 was noticed by the Supreme Court, in its subsequent judgment in Tutirorin Alkali Chemicals and Fertilizers Ltd.45, the law declared in Challapalli Sugars Ltd8, as explained in the subsequent judgment of the Supreme Court in Tutirorin Alkali Chemicals and Fertilizers Ltd.45, is binding on this Court. In order to guard against the possibility of inconsistent decisions on points of law by different Division Benches the rule has been evolved, in order to promote consistency and certainty in the development of the law and its contemporary status, that the statement of the law by a Division Bench is considered binding on a Division Bench of the same or lesser number of Judges. If the view expressed by two different Division Benches cannot be reconciled, the pronouncement of a Division Bench of a larger number of Judges should be preferred over the decision of a Division Bench of a smaller number of Judges. (Mattulal v. Radhelal ; Union of India v. Raghubir Singh ; Sakinala Hari Nath v. State of A.P.). Judicial discipline requires that the opinions expressed by larger benches of the Supreme Court, in preference to those expressed by smaller benches of the Supreme Court, should be followed. (Union of India v. K.S. Subramanian ; O.Ramachandra Reddi v. Director, D.R.D.L). When a decision rendered by a larger Bench of the Supreme Court is interpreted subsequently by a smaller Bench of the same Court, the lower Courts in the hierarchy have to follow the latter decision. (Sakinala Hari Nath50). The law declared in Challapalli Sugars Ltd.8, as explained in Tutirorin Alkali Chemicals and Fertilizers Ltd.45, is that, in the absence of a provision in the Income-tax Act indicating the contrary, the rules of accountancy or the Accounting Standards framed by the Institute of Chartered Accountants of India can be adopted. The question whether the increased wages payable under an award passed on 11.07.1983, subsequent to the end of the previous year from 01.07.1982 to 30.06.1983, can be claimed as a deduction in the said previous year, must be examined in the light of the provisions of the Income-tax Act, more so since the assessment year in question was long before Section 145 of the Income-tax Act was amended.

Section 2(34) of the Income-Tax Act, 1961, as it stood at the relevant time, defined previous year to mean the previous year as defined in Section 3. Section 3(1), as it then stood, defined previous year, for the purpose of the Income-tax Act, to mean (a) the financial year immediately preceding the assessment year; or

(b) if the accounts of the assessee had been made upto a date within the said financial year, then, at the option of the assessee, the 12 months ending on such date; or (c) in the case of any person or business or class of persons or business not falling within clause (a) or clause (b), such period as may be determined by the Board or by any authority authorised by the Board in this behalf. Section 4 related to charge of income-tax and, under sub- section (1) thereof, where any Central Act enacted that income-tax shall be charged for any assessment year at any rate or rates, income-tax at that rate or those rates shall be charged for that year in accordance with, and subject to the provisions of the Income-tax Act. Section 5 related to the scope of total income and under sub- section (1) thereof, subject to the provisions of the Income-tax Act, the total income of any previous year of a person who was a resident included all income from whatever source derived which

(a) was received or was deemed to be received in India in such year by or on behalf of such person; or (b) accrued or arose or was deemed to accrue or arise to him in India during such year; or (c) accrued or arose to him outside India during such year. Section 9 related to income deemed to accrue or arise in India. Section 28 of the Income Tax Act defined profits and gains of business or profession. Thereunder the following income was to be chargeable to income-tax under the head profits and gains of business or profession, (i) the profits and gains of any business or profession which was carried on by the assessee at any time during the previous year. Section 29, as it then stood, stipulated that the income, from profits and gains of business or profession, should be computed in accordance with the provisions contained in Sections 30 to 43(A).

The liability to pay tax, under the Income Tax Act, is with respect to amounts received and payments made in the previous year which, under Section 3(1) of the Income-tax Act, refers to a period of 12 months. An assessee that follows the mercantile system of accounting is entitled to deduct from the profits and gains of the business such liability which had accrued during the period for which the profits and gains were being computed. (Kedarnath Jute Mfg. Co. Ltd.11). Under the Income-tax Act, income charged to tax is the income that is received or is deemed to be received in the previous year relevant to the year for which assessment is made or on the income that accrues or arises, or is deemed to accrue or arise during such year. (Godhra Electricity Co. Ltd.13). If an income accrues within a particular year, it is liable to be assessed in the succeeding year. (A. Gajapathy Naidu20). The scheme of the Income-tax Act is that income-tax is assessed and paid in the next succeeding year upon the results of the year before. It is the income of the previous year which is brought to tax in the succeeding year, which is called the year of assessment. (C.I.T v. National Syndicate, Bombay ; Indian Iron & Steel Co. Ltd. v. Commissioner of Income-tax, Bengal). The income of the assessee should be determined according to the provisions of the Income-tax Act in consonance with the method of accountancy regularly employed by the assessee. The method of accounting regularly employed by the assessee helps computation of income, profits and gains under Section 28 of the Act, and the taxability of that income under the Income-tax Act must be determined. (State Bank of Travancore15). Entries in the books of accounts are not determinative or conclusive, and the matter should be examined on the touchstone of the provisions contained in the Income-tax Act (Kedarnath Jute Mfg. Co. Ltd.11; Tuticorin Alkali Chemicals & Fertilizers Ltd.45; Sutlej Cotton Mills Ltd. v. CIT ; United Commercial Bank v. CIT ; Taparia Tools Ltd.24). The previous year, for which the liability to tax is to be determined, would not undergo a change based on the Accounting Standards issued by the Institute of Chartered Accountant of India.

In Pact Securities and Financial Services Ltd.10, the appeals were preferred to this High Court, under Section 260A of the Income Tax Act, 1961, for the assessment years 1996-97 till 1999-2000. The assessing authority had disallowed deduction of lease equalisation charges from the lease rental income. Before the Division bench of this Court, reliance was placed by the assessee on the judgment of the Delhi High Court in CIT v. Virtual Soft Systems Ltd , and the Division bench of the Karnataka High Court in Prakash Leasing Ltd. v. Deputy CIT , to contend that similar questions fell for consideration before these High Courts; and, based on the guidance note issued by the Institute of Chartered Accountants of India, it was held that the assessees were entitled to determine equalisation charges from lease receipts; and the assessee was entitled to have its accounting policy, taking recourse to the guidance note issued by the Institute of Chartered Accountants of India, while accounting for lease transactions. On behalf of the revenue it was contended that, under Section 145(2) of the Income Tax Act, in the absence of a notification issued by the Central Government, neither the accounting standards nor the guidance note issued by the Institute of Chartered Accountants of India could be taken recourse to.

The Division bench of this Court, in Pact Securities and Financial Services Ltd.10, held that Section 145 of the Income Tax Act was substituted by Finance Act, 1995 with effect from April, 1st 1997; the assessment years, with which they were concerned, related to the period 1997-98 to 2000-2001; the Institute of Chartered Accountants of India had published a guidance note on accounting of leases in 1988, which was then revised in 1995; on April 1st 2001 the Institute of Chartered Accountants of India had published Accounting Standard No.19 in respect of leases; it was not in dispute that Accounting Standard No.19 was applicable, in respect of assets leased, during the accounting periods commencing on or after April, 1st 2001; the assessment years, under consideration in the appeals before them, were prior to April, 2001; the guidance note reflected the best practices adopted by Accountants in India; the Institute of Chartered Accountants of India was the authority to recommend Accounting Standards for ultimate prescription by the Central Government in consultation with the National Advisory Committee of Accounting Standards; notwithstanding the fact that the opinion of the Institute of Chartered Accountants of India was expressed in the guidance note, which had not attained a mandatory status, that would not provide the basis for the assessing authority to discard the books of account of the assessee even if, at the relevant time, it was not mandatory to adopt the methodology prescribed by the guidance note, or the accounting standards, as it was not notified by the Central Government in the official gazette; as long as there was a disclosure of the accounting policy in the accounts, which had the backing of professional bodies such as the Institute of Chartered Accountants of India, it could not be disregarded by the assessing authority; the accounting standards, prescribed by the Institute of Chartered Accountants of India, had received recognition of several decisions of the High Court and the Supreme Court; the proviso to Section 211(3C) of the Companies Act clearly specified that, till such time the Central Government so prescribed, the accounting standards, issued by the Institute of Chartered Accountants of India, shall be the relevant accounting standards; it was, therefore, not possible to read the words may employed in Section 145(2) of the Act as a wish; merely because the Central Government had not notified, in the Official Gazette, that the accounting standards would be followed by any class of assesses, or in respect of any class of income, it could not be stated that the accounting standards, prescribed by the Institute of Chartered Accountants of India or the accounting standards reflected in the guidance note, could not be adopted as an accounting method by an assessee; and notwithstanding the fact that the opinion of the Institute of Chartered Accountants of India was expressed in a guidance note, which had not attained mandatory status, was not a ground to discard the books of accounts of the assessee or the method of accounting for leases followed by the assessee, and for disallowing deduction towards lease equalisation charges from the lease rental income.

In Pact Securities and Financial Services Ltd.10, the assessment years in question were from 1996-97 to 1999-2000. The Division Bench of this Court, relying on Section 145 of the Income-tax Act and Section 211(3C) of the Companies Act, had held that the Accounting Standards framed by the Institute of Chartered Accountants of India would apply. Section 145 of the Income Tax Act, as substituted by the Finance Act, 1995, w.e.f. 1- 4-1997, related to the method of accounting. Under sub-section (1) thereof, Income chargeable under the head Profits and gains of business or profession or Income from other sources shall, subject to the provisions of sub-section (2), be computed in accordance with either cash or mercantile system of accounting regularly employed by the assessee. Sub-section (2) enabled the Central Government to notify, in the Official Gazette from time to time, accounting standards to be followed by any class of assesses or in respect of any class of income. Under sub-section (3), where the Assessing Officer was not satisfied about the correctness or completeness of the accounts of the assessee, or where the method of accounting provided in sub-section (1), or the accounting standards as notified under sub-section (2), had not been regularly followed by the assessee, the Assessing Officer could make an assessment in the manner provided in Section 144.

Prior to its substitution, Section 145(1), as amended by the Direct Tax Laws (Amendment) Act, 1987, w.e.f. 1-4-1988/1-4-1989 and the Finance Act, 1990, w.e.f. 1-4-1989, provided that the income, chargeable under the head Profit and gains of business or profession or Income from other sources, shall be computed in accordance with the method of accounting regularly employed by the assessee. Under the proviso thereto, in any case where the accounts were correct and complete to the satisfaction of the Assessing Officer but the method employed was such that, in the opinion of the Assessing Officer, the income could not properly be deduced therefrom, then the computation shall be made upon such basis and in such manner as the Assessing Officer may determine. Section 145(2) enabled the Assessing Officer, if he was not satisfied about the correctness or the completeness of the accounts of the assessee, or where no method of accounting has been regularly employed by the assessee, to make an assessment in the manner provided in Section 144.

Section 145 of the Income-tax Act, as it then stood, related to the method of accounting regularly employed by the assessee for his own purposes, and did not relate to a method of making up the statutory return of assessment to income-tax. Secondly, the Section clearly made such a method of accounting a compulsory basis of computation unless, in the opinion of the Income-tax Officer, the income, profits and gains could not properly be deduced therefrom. It may well be that, though the profit brought out in the accounts is not the true figure for income-tax purposes, the true figure can be accurately deduced therefrom. (The Commissioner of Income Tax, Bombay v. Sarangpur Cotton Manufacturing Co. Ltd., ; State Bank of Travancore15). Section 145 did not compel the Income-tax Officer to accept a balance- sheet of cash receipts and outgoings prepared from the books of account. It was for him to compute the income in accordance with the method of accounting regularly employed by the assessee. (State Bank of Travancore15; A. Krishnaswami Mudaliar16).

Section 210 of the Companies Act, 1956 related to annual accounts and balance sheet and, under sub-section (1) thereof, at every annual general meeting of a company, held in pursuance of Section 166, the Board of directors of the company were required to lay before the company (a) a balance sheet as at the end of the period specified in sub-section (3), and (b) a profit and loss account for that period. Section 210(3) stipulated that the profit and loss account shall relate (a) in the case of the first annual general meeting of the company, to the period beginning with the incorporation of the company and ending with a day which shall not precede the day of the meeting by more than nine months; and

(b) in the case of any subsequent annual general meeting of the company, to the period beginning with the day immediately after the period for which the account was last submitted and ending with a day which shall not precede the day of the meeting by more than six months, or in cases where an extension of time has been granted for holding the meeting under the second proviso to sub- section (1) of Section 166, by more than six months and the extension so granted. Section 210(4) stipulated that the period to which the accounts aforesaid related was referred to in the Companies Act as a "financial year"; and it may be less or more than a calendar year, but it should not exceed fifteen months. Under the proviso thereto, it may extend to eighteen months where special permission has been granted in that behalf by the Registrar of the Companies.

Section 210-A was inserted in the Companies Act, 1956, by the Companies (Amendment) Act, 1999, with effect from 31.10.1998. Sub-section (1) thereof enables the Central Government, by notification in the Official Gazette, to constitute an Advisory Committee to be called National Advisory Committee on Accounting Standards to advice the Central Government on the formulation and laying down of account policies and accounting standards for adoption by companies or class of companies under the Companies Act. Among others, the Advisory Committee was to consist of one member nominated by the Institute of Chartered Accountants of India. Sub-section (3) stipulated that the Advisory

Committee should give its recommendations to the Central Government, on such matters of accounting policies and standards and auditing, as may be referred to it for advice from time to time.

Section 211 of the Companies Act, 1956 related to the form and contents of the balance sheet and profit and loss account. Under sub-section (1) thereof, every balance sheet of a company should give a true and fair view of the state of affairs of the company as at the end of the financial year and shall, subject to the provisions of Section 211, be in the form set out in Part I of Schedule VI, or as near thereto as the circumstances admit, or in such other form as may be approved by the Central Government either generally or in any particular case; and in preparing the balance sheet due regard shall be had, as far as may be, to the general instructions for preparation of balance sheet under the heading "Notes" at the end of that Part. Sub-section (2) stipulated that every profit and loss account of a company should give a true and fair view of the profit or loss of the company for the financial year and shall, subject as aforesaid, comply with the requirements of Part II of Schedule VI, so far as they are applicable thereto.

Sub-sections (3A) to (3C) were inserted to Section 211 of the Companies Act, 1956 by the Companies (Amendment) Act, 1999 with effect from 31.10.1998. Sub-section (3A) stipulated that every profit and loss account and balance sheet of the company shall comply with the accounting standards. Sub-section (3B) stipulated that, where the profit and loss account and the balance sheet of the company did not comply with the accounting standards, such companies should disclose in its profit and loss account and balance-sheet, the following namely: (a) the deviation from the accounting standards; (b) the reasons for such deviation; and (c) the financial effect, if any, arising due to such deviation. Sub-section (3C) stipulated that, for the purpose of Section 211, the expression accounting standards meant the standards of accounting recommended by the Institute of Chartered Accountants of India constituted under the Chartered Accountants Act, 1949, as may be prescribed by the Central Government in consultation with the National Advisory Committee on Accounting Standards established under sub-section (1) of Section 210-A(1) of the Companies Act. Under the proviso thereto, the standard of accounting, specified by the Institute of Chartered Accountants of India, shall be deemed to be the accounting standards until accounting standards are prescribed by the Central Government under sub-section (3C) of Section 211.

In J.K. Industries Ltd. v. Union of India , the Supreme Court held that the scheme of the Companies Act indicated that accounting standards are made mandatory; they should be followed by the auditors, and by the companies; the accounting standards provide discipline and harmonisation of concepts and accounting principles; when accounting standards were not mandatory, various companies used to follow alternate systems of accounting; this led to over-statement of profits; therefore, the said standards have now been made mandatory; the Central Government has been entrusted the statutory function to frame accounting standards in consultation with the National Advisory Committee on Accounting Standards (NAC) under Section 211(3-C) of the Companies Act; it is not necessary for the Central Government to adopt, in every case, the accounting standards issued by the Institute of Chartered Accountants of India; nothing prevents the Central

Government from enacting its own accounting standards which may not be in consonance with the standards prescribed by the Institute; and, similarly, nothing prevents the Central Government from adopting the standards issued by that Institute.

The provisions of the Companies Act, as to the disposal of profits, are designed to protect the interests of the shareholders, and have no effect on the right which the State has under the provisions of the Income-tax Act to impose a tax on income when it arises or accrues. (Sree Meenakshi Mills Ltd.31). Accrual of income cannot be confused with its disposal. Income, which has accrued to an assessee, might remain undisposed of by him, but the liability to tax attaches to it, under the provisions of the Indian Income Tax Act, as soon as it accrues. It is no concern of the revenue how and when profits are disposed of by the assessee. (Sree Meenakshi Mills Ltd.31).

Section 145 was substituted in the Income-tax Act with effect from 01.04.1997, and sub-section (3C) was inserted into Section 211 of the Companies Act with effect from 31.10.1998, more than 12 years after the assessment year 1984-85 which is the relevant period with which we are concerned in the present case. As neither of these provisions were in the statute book during the relevant previous year 01.07.1982 to 30.06.1983, reliance placed on behalf of the asessee, on the judgment in Pact Securities and Financial Services Ltd.10 which had placed heavy reliance on the aforesaid two provisions to hold that Accounting Standards should be followed, is misplaced.

Even otherwise, the attention of the Division Bench of this Court, in Pact Securities and Financial Services Ltd.10, was not drawn to the judgment of the Supreme Court in Tuticorin Alkali Chemicals & Fertilizers Ltd.45. In any event the question whether Accounting Standard-4 can be applied, even if it results in increasing the previous year beyond a period of 12 months, did not arise for consideration in Pact Securities and Financial Services Ltd.10. Reliance placed on this judgment is, therefore, of no avail.

In Nagri Mills Co. Ltd.6, on which reliance is placed on behalf of the assessee, the Bombay High Court held that the question, as to the year in which a deduction is allowable, may be material when the rate of tax chargeable on the assessee in two different years is different; but in a case where, on the income of a company, tax is attracted at a uniform rate it would be of no consequence to the department whether the deduction in respect of bonus was granted in the assessment year 1952-53 or in the assessment year corresponding to the accounting year 1952 i.e in the assessment year 1953-54; and the Department should not fritter away its energies in fighting matters of this kind.

The judgment of the Bombay High Court, in Nagri Mills Co. Ltd.6 was followed in Shri Ram Pistons and Rings Ltd.7 wherein the Delhi High Court held that, in the reference before them, there was no doubt that the assessee had incurred the expenditure; the only dispute was regarding the date on which the liability had crystallized; it appeared that there was no change in the rate of tax for the assessment year 1983-84 with which they were concerned; the question, therefore, was only with regard to the year of deduction;

and it was a pity that the Court had to expend so much time and energy only to determine the year of taxability of the amount.

The contention, based on the aforesaid judgments of the Bombay and Delhi Courts, that it matters little whether the liability is to be determined with respect to a particular previous year or the next, is only to be noted to be rejected. If the language of a provision in a taxing statute is plain and unambiguous, the provisions thereof must be enforced and it is, normally, not the concern of Courts to examine its reasonableness or consider its consequences. In a taxing statute one has to look at what is clearly said. There is no equity about a tax. There is no intendment. There is no presumption as to a tax. Nothing is to be read in, nothing is to be implied. One can only look fairly on the language used (Cape Brandy Syndicate v. IRC). If the meaning of the provision is reasonably clear, Courts have no jurisdiction to mitigate harshness. (Canadian Eagle Oil Co. Ltd v. R ; IRC v. Ross & Coulter (Bladnock Distillery Co. Ltd ; The State of A.P. v. M/s.Gouri Shankar Modern Rice Mill).

The doctrine, that in taxation cases, the subject is to be taxed if, in accordance with a Court's view of what it considers the substance of the transaction, the Court thinks that the case falls within the contemplation or spirit of the statute, must be viewed with disfavour. The subject is not taxable by inference or by analogy, but only by the plain words of a statute applicable to the facts and circumstances of his case. (J.K. Steel Ltd. v. Union of India ; Inland Revenue Commissioners v. Duke of Westminister). The principle of all fiscal legislation is this: If the person sought to be taxed comes within the letter of the law he must be taxed however great the hardship may appear to the judicial mind to be. On the other hand, if the Crown, seeking to recover the tax, cannot bring the subject within the letter of the law, the subject is free, however apparently within the spirit of the law the case might otherwise appear to be. (Partington v. Attorney-General ; J.K. Steel Ltd.65).

In construing fiscal statutes, and in determining the liability of a subject to tax, one must have regard to the strict letter of the law and not merely to the spirit of the statute or the substance of the law. If the Revenue satisfies the Court that the case falls strictly within the provisions of the law, the subject can be taxed. If. on the other hand, the case is not covered within the four corners of the provisions of the taxing statute, no tax can be imposed by inference or by analogy or by trying to probe into the intentions of the legislature and by considering what was the substance of the matter. (Diwan Bros. v. Central Bank of India ; A.V. Fernandez v. State of Kerala).

Courts of law have nothing to do with the reasonableness or unreasonableness of a provision of a statute except so far as it may help it in interpreting what the legislature has said. If the language of a statute be plain, admitting of only one meaning, the legislature must be taken to have meant and intended what it has plainly expressed, and whatever it has in clear terms enacted must be enforced though it should lead to absurd or mischievous results. If the language of the Section be not controlled by some of the other provisions of the Statute, it must, since its language is plain and unambiguous, be enforced, and the Court is judicially not concerned with the question whether the policy it embodies is wise or unwise, or whether it leads to consequences just or unjust, beneficial or mischievous. (Cooke v. Charles A. Vogeler Co. ; M/s. Gouri Shankar Modern Rice Mill64).

As long as there is no ambiguity in the statutory language, resort to any interpretative process to unfold the legislative intent becomes impermissible. The supposed intention of the legislature cannot then be appealed to whittle down the statutory language which is otherwise unambiguous. If the intendment is not in the words used it is nowhere else. The need for interpretation arises when the words used in the statute are, on their own terms, ambivalent and do not manifest the intention of the legislature. Artificial and unduly latitudinarian rules of construction which, with their general tendency to give the taxpayer the breaks, are out of place where the legislation has a fiscal mission. (Keshavji Ravji & Co. v. CIT ; M/s.Gouri Shankar Modern Rice Mill64).

Individual cases of hardship and injustice do not, and cannot, have any bearing for rejecting the natural construction by attributing normal meanings to the words used. A fiscal statute should be interpreted on the language used therein, and not dehors the same. No words ought to be added and only the language used ought to be considered so as to ascertain the proper meaning and intent of the legislation. The Court is to ascribe natural and ordinary meaning to the words used by the legislature and the Court ought not, under any circumstances, to substitute its own impression and ideas in the place of the legislative intent as is available from a plain reading of the statutory provision. (M/s.Gouri Shankar Modern Rice Mill64; Orissa State Warehousing Corporation v. CIT).

The provisions of fiscal statutes must be strictly construed and, if the assessee falls within the letter of the law, he must be taxed. His liability to pay tax cannot be determined relying on its possible consequences of whether or not it would make any difference if the deduction is claimed in one year or the other. The consequences of the liability being held to arise in a previous year, different from the previous year in which the liability actually arose, are many. It is wholly unnecessary for us to make a detailed analysis of such consequences as the Income-tax Act makes an assessee liable to tax on the income which accrued in his favour in the previous year; and, in determining such income, the liability/expenditure incurred in such a previous year alone should be take into consideration. Question No.1 is answered in the negative, against the assessee and in favour of the Revenue. QUESTION No.2:

The assessee claimed deduction of Rs.99,17,273/- towards commission payable to two agents in Sri Lanka. While scouting for an order in Sri Lanka, the assessee had appointed Eastern Trading Co. Ltd and Globe Commercial Agencies Ltd. as its agents, for procuring orders, by two agreements both dated 25.07.1981. On examining the contents of the agreement, the Income Tax Officer held that they provided a formula for quantification of the commission according to which the commission was payable only in respect of supplies made during the year. He computed the commission payable during the year at Rs.14,211/-, on the supplies of machinery for Rs.22,84,234/-, and disallowed the balance of Rs.99,03,062/-. This order of the Income-tax Officer was confirmed in appeal. In further appeal, the Tribunal held that the issue had to be decided on the effect of Clause (d) of the agreement; under Clause (d) the consideration was to arise only on the assessee securing the orders, and consequently the liability to pay commission arose on that date; sub-clause (a) provided only for the manner of computation of commission on the basis of FOB value, which was also specified in the contract approved by the Reserve Bank; accrual of liability was under clause (d), while computation of the amount of commission was under Clause (a); and merely because the actual payment was staggered, by mutual agreement, did not affect accrual of liability. The Tribunal allowed deduction, of the entire accrued liability, without reference to the actual payment holding that the assessee was following the mercantile system of accounting.

Sri J.V. Prasad, Learned Senior Standing Counsel for Income-tax, would submit that accrual of liability of the asseseee, to pay commission to its agents, rests on the respective agreements entered into between the assessee on the one hand and the two agents, viz., Eastern Trading Co. Ltd., and Globe Commercial Agencies Ltd., on the other; all the terms of the agreement should be read together to ascertain when, or at what point of time, the assessee became legally liable to make payment towards commission; the assessee became legally due, in respect of a percentile of the commission to be paid to the agent, on the value of the goods supplied during the previous year to its Sri Lankan agents; the value of the goods, supplied during the relevant previous years, was Rs.2,84,234/-; the assessee became legally obligated to pay the agent commission of 1% on the FOB value, and hence the said amount alone could be allowed as a deduction; the Tribunals finding is that the agent became entitled to payment of commission, on the full value of the goods, as the order was secured during the previous year, and Clause (d) of the agreement speaks of commission on securing the order; the Tribunal failed to read all the sub-clauses of Clause 4 together, in fixing the point at which the legal liability arises; the question that the Tribunal ought to have posed, and answered, is whether the agent had acquired a legal right to sue the assessee, for payment of the entire commission, the moment the order was secured, and whether the plaintiff would succeed in law if the suit was based only on Clause 4(a), and clause 4(d) were to be ignored; and the answer would have been in the negative as, while Clause 4(d) only enjoins payment of commission on securing the order, the right to receive commission is governed by sub-clause (a) of Clause (4).

On the other hand Sri S. Ravi, Learned Senior Counsel, would submit that the Tribunal, after interpreting the agreements entered with the Eastern Trading Co. and Globe Commercial Agencies Ltd., had held that the liability to pay commission arose immediately upon securing the order; admittedly the orders were secured; therefore, the liability to pay commission accrued on the date of securing the orders; and though payment of commission, as per the agreements, is to happen at a later date, since the liability had accrued, and became enforceable, the Assessee was entitled to claim deduction.

Before we consider the rival submissions, it is useful to take note of the relevant clauses of the two agreements which read as under:

Eastern Trading Co. Ltd.

In consideration of the above services and on K.C.P. securing the contract

(a) Agent will be paid a consideration of 1% on the FOB value of Machinery and Equipment supplied for the Sugar Corporation and also on the consideration received by K.C.P. for services rendered in Sri Lanka towards Civil Works and Erection. No commission is payable on taxes/levies, customs duty (if payable/levies, freight/transport charges.

(b) Within 15 days of K.C.P. getting the first advance from the customer, U.S. Dollars 5,00,000/- (Five hundred thousand U.S. Dollars) will be paid to the Agent. Balance Commission will be paid on mutually agreed instalment.

(c) Agent will meet all incidental expenses till the contract is awarded .

(d) Consideration referred to above arises only on K.C.P. securing the order. Till then each party will bear their respective expenses.

Globe Commercial Agencies Ltd.

In consideration of the above services, and on K.C.P. securing the contract:-

(a). M/s. Globe Commercial Agencies will be paid a consideration of 1 % on the FOB value of the machinery and equipment supplied to the Sugar Corporation and also on the consideration received by K.C.P. for services rendered in Sri Lanka towards Civil Works and Erection. No commission is payable on taxes/levies, customs duty (if payable)/levies, freight/transport charges.

(b). The payment will be made in proportion to the payments received by K.C.P.

(c). Messers. Globe Commercial Agencies will meet all incidental expenses for obtaining this contract.

(d). The commission shall be paid to Messers. Globe Commercial Agencies or their nominees in Sri Lanks.

(e). Consideration referred to above arises only on K.C.P. securing the order. Till then each party will bear their respective expenses.

The question whether liability has arisen to the assessee, during the relevant previous year, must be determined on a reading of the clauses in the agreement as a whole, and not piece meal. While the assessees agents had secured an order during the previous year, relevant to the assessment year 1984-85, supplies were effected in the subsequent previous years. The agreement entered into by the assessee with its two agents in Sri Lanka viz., Eastern Indian Company Limited and Global Commercial Agencies Limited must, therefore, be read as a whole to determine when the liability of the assessee, to pay commission to these two agents, arose. A plain reading of the relevant clauses in the agreement, entered into between the assessee and Global Commercial Agencies, shows that the agent was to be paid consideration of 1% on the FOB value of the machinery and equipment supplied by the assessee to the Sugar Corporation, and also on the consideration received by the assessee for services rendered in Sri Lanka towards erection and civil works. Payment of commission was required to be made only after supplies were made by the assessee to the Sugar Corporation. Clause (d) stipulated that the commission shall be paid to the agents or their nominees in Sri Lanka. Clause (e) is relevant. It stipulated that the consideration, as referred to in the earlier clauses, would arise only on the assessee securing the order. It is evident therefore that, while the liability of the assessee to pay commission to its agents accrued, in terms of clause (e), on the agent securing the order, actual payment of commission was to be made, at 1% of its FOB value, on the supply of machinery and equipment to the client as well as on the consideration received by the assessee for services rendered by them for erection and civil works.

As the assessee maintained its books of accounts, under the mercantile system of accounting, their liability to pay commission to the agents arose in the relevant previous year in which the agent secured the order; and as, in the present case, both the agents had secured orders from the clients in Sri Lanka, during the previous year relevant to the assessment year 1984-85, the Tribunal has, in our view rightly, held that the liability to pay commission accrued when the orders were secured by the agents, and not when supplies were effected by the assessee. This question is answered in the affirmative, in favour of the assessee, and against the Revenue.

QUESTION No.3:

The assessee had claimed weighted deduction, under Section 35-B of the Income-tax Act, with respect to payment of commission of Rs.33,05,758/-. This claim was rejected by the Income-tax Officer holding that Section 35-B was itself omitted from 01.03.1983; even if that Section was applied, the assessee was not eligible under any of the clauses thereunder; the assessee could not be regarded as maintaining an agency outside India, the expenditure did not fall within the prescribed category; and since he had restricted the commission, admissible as deduction, to Rs.14,211/-, weighted deduction would be available only for 1/3rd thereof i.e. Rs.4,737/-. In appeal, the CIT (Appeals) held that procuring a contract abroad did not amount to export development; and, accordingly, confirmed the disallowance.

In further Appeal, the Tribunal held that Section 35-B ceased to apply with respect to the expenditure incurred after 01.03.1983; it was, therefore, necessary to ascertain whether the expenditure was incurred before that date, and whether it fell within item (iv) of Section 35-B(1)(b) of the Income-tax Act; under the agreements, the assessee had maintained an agency in Sri Lanka for the purpose of representing it in developing the export market for its services; the expenditure, therefore, fell within the scope of item (iv); and the assessee had paid 5,00,000 U.S. Dollars, equivalent to Rs.45,00,000/-, to its agent on 16.12.1982, with the permission of the Reserve Bank of India, before the Section was repealed on 01.03.1983. The claim of the assessee, for weighted deduction, was allowed.

With regards the contention of the Revenue that appointment of an agent for a particular purpose could not be regarded as maintaining an agency, within the meaning of item (iv) of Section 35-B(1)(b) of the Income-tax Act, the Tribunal opined that this question involved interpretation of the phrase maintaining an agency outside India, and this question should be referred for the opinion of the High Court.

Sri J.V. Prasad, Learned Senior Standing Counsel for Income-Tax, would submit that Section 35B, which was inserted w.e.f. 01.04.1968 and which underwent subsequent amendments, was omitted w.e.f. 01.04.1983; the said provision pertained to deduction of allowances to encourage development of Export Markets; the assessee claimed deduction of Rs.33,05,758/-, representing 1/3rd of Rs.99,17,273/-, which the assessee claimed was the commission payable to the two Sri Lankan agents; the assessee had claimed the said sum as allowable, under Section 35B(1)(b)(iv), contending that it had maintained an agency outside India, they had paid commission to the agents, and were therefore eligible for an allowance of 1/3rd of the said commission; the assessing officer and the CIT(A) had disallowed the claim; the Tribunal had allowed the claim relying on the order of the Allahabad Bench of the Tribunal in Kothari Carriers v. ITO , wherein it was held that maintenance of an agency meant an act of continuing the relationship of principal and agent; Section 35B(1)(b)(iv) speaks of allowance in respect of expenditure incurred for the maintenance of a branch, office or agency for the promotion of sale outside India of such goods, services or facilities; a plain reading of Section 35-B would, unambiguously, show that the assessee is not entitled for the deduction; the Tribunal erred in allowing the same by a perfunctory order; in order to claim the benefit, the assessee must have firstly incurred some expenditure; such expenditure should have been incurred towards maintenance of (i) a branch, (ii) office, or (iii) an agency; that apart, such expenditure should be for the promotion of the sale of goods, etc; the agency, referred to in Section 35-B, is synonymous with the words branch and office; it would thus, generally, indicate a tangible structure with staff equipment, etc., which requires regular maintenance; the principle of ejusdem generis should be applied to understand the meaning and intent of granting such an allowance; facts assume importance in the context of this claim; the assessee sought deduction on the commission paid to the agents; firstly, the expenditure contemplated in the provision is not the same as commission paid to agents; secondly, there is no claim by the assessee of having incurred any expenditure on an agency; thirdly, the commission paid is not in respect of any specified amount required to be spent by the agents in running their agency, but is in respect of commission paid to agents to secure a contract; and it is thus clear that the assessee has not made out any case for weighted deduction.

With regards the judgment of the Supreme Court, in Velvet Carpet & Co. Ltd. v. CIT, Allahabad on which reliance was placed on behalf of the respondent-assessee, Sri J.V.Prasad, Learned Senior Standing Counsel for Income-Tax, would submit that the said decision is based on its own facts, and has not considered the question that arises herein; that apart, the provision extracted in the judgment would show that it is slightly different in its wording i.e., agent is reflected, instead of agency; there is also no discussion regarding the nature of expenditure that is allowable, under the provisions, in the said judgment; sub- section (2) of Section 35B of the Act also acts as a bar; and, as held by the

Supreme Court in CIT v. Stepwell Industries Ltd. , each case must be examined in the light of the statutory provisions, and the facts.

On the other hand Sri S.Ravi, Learned Senior Counsel, would submit that the assessee claimed weighted deduction, under Sec.35B(1)(b)(iv) of the Income Tax Act, for the expenditure incurred towards payment of commission to Sri Lankan Agents; the aforesaid provision specifies that any expenditure, incurred on the maintenance of any branch, office or agency outside India for the promotion of sales, shall be entitled for a weighted average deduction at 1 and 1/3rd times that expenditure; the assessee had an agreement with two Sri Lankan agencies to act as their agent for procuring business in Sri Lanka; having succeeded in the same, and upon the issuance of purchase orders, the said agents were entitled for a commission in terms of the agency agreement; and the question whether the expenditure incurred, on account of commission paid to an agent outside India, would qualify to claim weighted average deduction under Section 35B(1)(b)(iv), fell for consideration, in CIT v. Usha Telehoist Ltd. and Velvet Carpet & Co. Ltd.74, and is no more res-integra.

It is useful, in this context, to refer to Section 35-B as it then stood, which read as follows:

S.35B. Export Markets development allowance (1) (a) Where an assessee, being a domestic company or a person(other than a company) who is resident in India, has incurred after the 29th day of February, 1968 (but before the 1st day of March, 1983) whether directly or in association with any other person, any expenditure (not being in the nature of capital expenditure or personal expenses of the assessee) referred to in clause (b), he shall, subject to the provisions of this section, be allowed a deduction of a sum equal to one and one-third times the amount of such expenditure incurred during the previous year. (provided that in respect of the expenditure incurred after the 28th day of February, 1973) (but before the 1st day of April, 1978,) by a domestic company, being a company in which the public are substantially interested, the provisions of this clause shall have effect as if for the words one and one-third times, the words one and one-half times had been substituted.)

(b) The expenditure referred to in clause (a) is that incurred wholly and exclusively on

(i) advertisement or ..

(iv) maintenance outside India of a branch, office or agency for the promotion of the sale outside India of such goods, services or facilities;

(vii) travelling.

(ix) such other activities.

(Explanation 1) In this section, domestic company shall have the meaning assigned to it in clause (2) of Section 80B.

(Explanation 2) For the removal of doubts, it is hereby declared that nothing in clause (b) shall be construed to include any expenditure which is in the nature of purchasing and manufacturing expenses ordinarily debatable to the trading or manufacturing account and not to the profit and loss account) ((1A)****) (2) Where a deduction under this Section is claimed and allowed for any assessment year in respect of any expenditure referred to in sub-section (1), deduction shall not be allowed in respect of such expenditure under any other provision of this Act for the same or any other assessment year.

While the commission actually paid to agents is required to be deducted as an expenditure in determining the income of the assessee for the previous year, Section 35-B of the Income Tax Act, as it then stood, provided for weighted deduction in certain circumstances. Under Section 35B(1)(b)(iv) of the Income Tax Act a weighted deduction of 1 and 1/3rd of the expenditure incurred during the previous year was eligible as deduction from the income of the previous year. Section 35-B(1)(b)(iv) stipulated that the expenditure, referred to in Section 35-B(1)(a), was the expenditure incurred wholly and exclusively on the maintenance outside India of a branch, office or agency for the promotion of the sale outside India of such goods, services or facilities. The weighted deduction under Section 35-B(1)(a), for a sum equal to 1 and 1/3rd times the amount of expenditure, was available only if such expenditure (i) had actually been incurred in the previous year; (ii) such expenditure had been incurred wholly and exclusively on the maintenance of an agency outside India; (iii) such an agency outside India had been maintained by the assessee for the promotion of sales outside India of its goods, services and facilities.

It is not in dispute that the assessee had two agents in Sri Lanka to procure orders from Sri Lanka clients for the supply of machinery and equipment by the assessee to them. The assessee had claimed weighted deduction for the U.S. Dollars 5,00,000/- (Five hundred thousand U.S. Dollars) which it had paid as advance commission to its agent M/s. Eastern Trading Company Limited. The contention of the revenue was that payment of advance of U.S. Dollars 5,00,000/- (Five hundred thousand U.S. Dollars) to M/s. Eastern Trading Company Limited did not satisfy the requirements, of Section 35-B(1)(b)(iv), for being granted weighed deduction.

The agreement with M/s. Eastern Trading Company Limited stipulated that the agent should meet all incidental expenses till the contract was awarded. Except for payment of commission of a particular percentage of the FOB value of the machinery and equipment to be supplied, the assessee was not liable for any other expenditure incurred by their agent in Sri Lanka. The contention of the revenue is that the word maintaining an agency required the expenditure to have been incurred for maintaining an agency outside India, that too for the promotion of sale outside India of the goods of the assessee.

In order to ascertain whether the assessee was maintaining an agency we must first examine what the word maintain means? The dictionary meaning of the word maintain is to carry on, to keep up, to support. The word maintenance means to support, and it is only if the contractual terms require the assessee to incur expenditure to support its agent in Sri Lanka, can it then be said to have maintained an agency. As noted hereinabove, the requirement of the aforesaid provision is not only that the assessee should have maintained an agency, but also that maintenance of an agency must be for the promotion of sale of the assessees goods outside India. The word promotion is an act of promoting, encouraging, an effort to publicize and increase the sales of a particular product. It is only in cases where the contract entered into between the assessee and its agent requires the assessee to maintain an agency, and requires the agent to publicise the goods of the assessee for the purpose of increasing its sales, would the expenditure incurred, towards promotion of sale of the assessees goods, be entitled for weighted deduction. Payment of 500,000 US dollars by the assessee to its agent is only the advance commission payable on the agent securing the order for supply of machinery and equipment from a client in Sri Lanka, and not for sales promotion. No obligation is placed on the agent, under the terms and conditions of the agreement, to promote sale of the assessees goods, nor does it require the assessee to reimburse any such expenditure. Likewise the agreement does not require the assessee to incur any expenditure to support its agent in Sri Lanka, and the commission required to be paid is only on the agent securing orders. The contractual terms, in fact, require the agent to incur all incidental expenditure for obtaining the contract. We find considerable force in the submission of Sri J.V. Prasad, Learned Senior Standing Counsel for Income Tax, that appointment of an agent and paying him commission only for procuring orders for the assessee to supply goods, does not, by itself, fulfill the requirements of Section 35B(1)(b)(iv); and it is only if the assessee incurs expenditure in the maintenance of an agency, that too for promotion of sale outside India of its goods, would the assessee be eligible to claim weighted deduction on the expenditure incurred in this regard. The expenditure incurred towards payment of commission for procuring orders, cannot be equated to expenditure incurred for maintaining an agency for promotion of sales, outside India, of the assessees goods.

In Velvet Carpet & Co. Ltd.74 the question which fell for the consideration of the Supreme Court was whether the appellant/assessee was entitled to weighted deduction, in terms of Section 35B(1)(b)(iv) of the Income Tax Act, 1961, which was the provision in force during the relevant period. In the return filed by the assessee for that year, it had stated that a sum of Rs. 4,60,433/- was paid by them to Mr. Jack Barouk of Brussels who was appointed by the assessee as its commercial agent in the said country for the sale of the assessee's goods; Section 35B(1)(b)(iv) provided for weighted deduction that was, in addition to the actual amount spent, one-third thereof as an additional expenditure, which provision was introduced to give benefit to the assessee. The Supreme Court held that as per Section 35B(1)(b)(iv) the expenditure incurred shall qualify for weighted deduction in case the expenditure is incurred wholly and exclusively on maintenance outside India of a branch, office or agent for the promotion of the sale outside India of such goods, services or facilities; what was not in dispute was that the expenditure was in fact incurred; it was also incurred wholly and exclusively outside India as the payment was made to Mr. Jack Barouk a resident of Brussels; it is also not in dispute that this payment was made against some sales of carpets belonging to the assessee, made by the said Mr. Jack Barouk; the only dispute was whether he could be treated as agent of the assessee; a perusal of the judgment of the ITAT revealed that the ITAT had looked into the agreement that was entered into between the assessee and the aforesaid Mr. Jack Barouk, and found that this agreement was an agency agreement; the ITAT also took into consideration another supporting fact that, as per the legal requirement, the said agreement was approved by the Reserve Bank of India, and the Reserve Bank of India, in its approval, had treated this agreement to be an agency agreement; the High Court, while allowing the appeal of the Department and rejecting the claim of the assessee, had observed that, at no stage, the assessee had put up a case that it had maintained a branch or agency outside the country; this was clearly an erroneous finding and against the record; no doubt, the assessee was not maintaining any branch office; however, the case of the assessee was that Mr. Jack Barouk was appointed as his agent; and it was the specific case made out by the assessee right from the stage of the assessment proceedings, it was specifically argued before the ITAT, and was accepted by the ITAT.

A judgment is a precedent binding on a co-ordinate bench, or a lower Court, only for the ratio laid down therein. Observations of Courts are neither to be read as Euclids theorems nor as provisions of a Statute, and that too taken out of their context. (Amar Nath Om Prakash v. State of Punjab ; CCE v. Alnoori Tobacco Products ; London Graving Dock Co. Ltd. v. Horton ; Home Office v. Dorset Yacht Co. ; Shepherd Homes Ltd. v. Sandham British Railways Board v. Herrington). The decision of a Court is only an authority for what it actually decides. What is of the essence in a decision is its ratio, and not every observation found therein nor what logically follows from the various observations made in it. (State of Orissa v. Sudhansu Sekhar Mistra Hegde ; Quinn v. Leathem).

In Velvet Carpet & Co. Ltd.74, the Supreme Court held that the ITAT had looked into the agreement between the assessee and its agent; and the said agreement had been approved by the Reserve Bank of India which had treated the agent as an agency agreement. As held by the Supreme Court, in Velvet Carpet & Co. Ltd.74, the question whether the assessee is entitled for weighted deduction would depend on whether or not its agreement with its agent fulfils the conditions stipulated in Section 35- B(1)(b)(iv) of the Income-tax Act.

In Stepwell Industries Ltd.75, the Supreme Court held that, in order to qualify for deduction, the expenditure must have been wholly or exclusively incurred for the purposes mentioned in sub- clause (b) of Section 35-B(1); the claim of the assessee, for weighted deduction under Section 35-B, cannot be allowed without going into the facts of the case; the onus of proving the facts, and getting the benefit of deduction, lay on the assessee; and the Tribunal could not allow the claim on assumption of facts.

As noted hereinabove neither does the agreement, between the assessee and its Sri Lankan Agent, disclose fulfillment of the ingredients of Section 35-B(1)(b)(iv), nor was the payment of 500,00 U.S dollars, by the assessee to its agent, made for any expenditure incurred in the promotion of the sale outside India of the assessees goods. In the present case, the assessee has not discharged the onus of establishing that the expenditure was wholly or exclusively incurred for the purposes mentioned in Section 35-B(1)(b)(iv) of the Act. The Tribunal fell in error in holding otherwise. This question is answered in the negative, in favour of the Revenue, and against the assessee. QUESTION No.4:

The assessee had claimed deduction of Rs.15,45,932/- as the insurance premium payable for a policy to cover all risks in erection of the project in Sri Lanka. This claim of deduction was disallowed by the Income-tax Officer on the ground that the insurance premium had not been paid, and had been shown as outstanding in the accounts as on 30.06.1983. With respect to another policy, the assessee had claimed only the pro-rata amount, referable to the period of the policy falling within the previous year, carrying over the balance as pre-paid expenditure. The Income-tax Officer, accordingly, worked out the pro-rata amount noting that the period covered was from 14.03.1983 to 31.03.1985, i.e for a period of 745 days. The cover within the previous year being 75 days, he allowed a sum of Rs.1,55,625/-, and added back the balance of Rs.13,90,307/-. In appeal, the CIT (Appeals) held that the policy was actually taken after the end of the previous year with retrospective effect, and there was no liability at all during the previous year. Accordingly, he enhanced the assessment by disallowing the entire amount of Rs.15,45,932/-.

In further appeal, the Tribunal held that the assessee, as a contractor, was bound to take an insurance policy to cover the risk from the date of commencement of the work which was on 14.03.1983; even though the policy was issued on 16.06.1983, it covered the period from 14.03.1983 to 13.03.1985, and from 14.03.1985 to 13.03.1986; the terms of the insurance policy showed that the assessee had incurred the liability to pay the premium, but had been permitted to pay the same subsequently; even though the indemnity was subject to payment of premium, the policy itself came into operation from 14.03.1983; the liability to pay the premium also arose on that date as mutually agreed; and the assessee had been reimbursed to the extent of Rs.9,19,995/-, and the amount charged in the account was only Rs.6,25,937/- which was the difference between the premium payable of Rs.15,45,932/- and the reimbursed amount. The Tribunal allowed the deduction.

Sri J.V. Prasad, Learned Senior Standing Counsel for Income-Tax, would submit that the insurance policy was taken after the end of the previous year with retrospective effect, and there was no liability; the said policy itself stipulated that it would come into force only on payment of the premium; and, admittedly, the premium was not paid during the relevant previous year.

On the other hand Sri S. Ravi, Learned Senior Counsel, would submit that the insurance premium, payable under the policy to cover risks in erection of the projects in Sri Lanka amounting to Rs.15,45,932/-, was claimed as a deduction by the assessee; the said Policy was issued on 16.06.83, however covering the period 14.03.1983 to 31.03.1985; the total premium was payable, in four instalments, starting from the inception; as the assessee had incurred the liability as per the policy, it got reimbursement from the Government of Srilanka; the liability had arisen even though premium was paid in instalments; and therefore, following the same accrual basis, the Assessee has been rightly allowed deduction.

The assessee claimed deduction towards insurance policy premium of Rs.15,45,932/-. The insurance was to cover all risks in the erection of the project in Sri Lanka. While the insurance cover started from 14.03.1983, and was extended upto 13.03.1985, the assessee did not pay the premium before the end of the previous year i.e by 30.06.1983; and the entire premium payable of Rs.15,45,932/- was shown as an outstanding liability in the balance-sheet of the assessee as on 30.06.1983. The Insurance Corporation of Sri Lanka had also addressed a letter to the assessee on 30.06.1983 requesting it to pay the premium.

While the assessing authority treated it as a mere provision, and not as a liability which had accrued during the previous year ending 30.06.1983, the assessee contended that, since the insurance cover started from 14.03.1983, and the policy was issued on 16.06.1983 (with retrospective effect from 14.03.1983), both of which fell within the previous year 01.07.1982 to 30.06.1983, the liability to pay the insurance premium arose during the previous year relevant to the assessment year 1984-85. The assessee further stated that they were granted the facility for payment of insurance premium in four installments on 14.03.1983, 14.09.1983, 14.03.1984 and 14.09.1984; the insurance cover thus started from 14.03.1983; it was a single premium policy; since the date of both the insurance policy and the insurance cover fell within the relevant accounting period, the assessee was entitled for deduction of the insurance premium, as it maintained its accounts on the mercantile system of accounting; and the fact that the insurance premium was actually paid only in the subsequent previous years was of no consequence.

It is no doubt true that, since the assessee maintained its books of accounts under the mercantile system of accounting, it was entitled to claim deduction of a liability on the date of its accrual, and not on the date of its actual payment. The assessee may, therefore, be justified in contending that the mere fact that the insurance premium was paid in the subsequent previous years, and not in the previous year 01.07.1982 to 30.06.1983, was not relevant. The question which, however, necessitates examination is when the liability of the assessee arose. The terms and conditions of the agreement, entered into by the assessee with the Insurance Corporation of Sri Lanka, stipulated that the policy of insurance was subjected to the insured having paid to the insurer the premium mentioned in the schedule; and subject to the terms, exclusions, provisions and conditions etc. The terms and conditions of insurance were subject to fulfillment of the basic condition of the insured having paid to the insurer the premium mentioned in the schedule to the policy. While the insurance policy was, no doubt, made applicable with retrospective effect from 14.03.1983, the date on which the liability arose must be determined on reading the terms and conditions of the policy as a whole. The transaction as it has been recorded in the books of accounts, under the mercantile system of accounting or the double entry system, is neither metamorphosed nor does the relationship between the parties assume a different character. The relationship as between the parties to the agreement still subsists and there does not come into existence a new relationship as between the parties with all its necessary consequences. (Keshav Mills Ltd.29).

In a case of supply of goods, merely because the goods have been supplied and the price thereof has been debited to the purchaser, the rights and obligations of the vendor and purchaser inter-se are not in any manner affected. The vendor is bound to fulfil all his obligations under the contract, and continues to be liable for all the consequences of his default including rejection of his goods by the purchaser or a claim for damages for breach of warranty by him. The purchaser is equally entitled to reject the goods or to claim the damages as on breach of warranty by the vendor, and all these rights and obligations should be worked out inspite of the fact that the entries are made in the books of accounts by the vendor in accordance with the mercantile system of accounting adopted by him. The vendor cannot say that he is under no further obligation to the purchaser, and that the purchaser must pay the price of the goods debited to him as a debt arising out of the book entry. The count in any action filed by the vendor against the purchaser would be a count for the price of the goods sold and delivered, and would not be a count on an assumption for recovery of a debt due by the debtor to him. (Keshav Mills Ltd.29).

Since the basic condition stipulated in the insurance policy is that the terms and conditions of the policy would apply only on the insured (assessee) having paid the insurance premium, the insurance coverage depended on the assessee making payment of the insurance premium. While the assessee was given the facility of payment of premium in four installments, and the first such installment was required to be paid on 14.03.1983, the fact remains that the assessee did not even pay the first installment, of the insurance premium, before 30.06.1983, the last date of the relevant previous year; and, since even the first installment was not paid, the insurance cover under the policy was not available to the assessee during the previous year 01.07.1982 to 30.06.1983. While in a cash system of accounting, deduction can be claimed only on the date on which payment is actually made, and not on the date on which the liability accrued, in a mercantile system of accounting the liability arises on the date of its accrual. This date of accrual must be ascertained on a reading of the terms and conditions of the underlying contract. It is possible for the terms and conditions of the contract to stipulate that the date on which the amount is paid is the date on which the liability accrued.

For instance, under the very same insurance policy, if the risk, for which the policy was taken, had occurred before 30.06.1983, the assessee would not have been entitled to claim insurance for the damage or loss suffered by it, since the conditions of the insurance policy explicitly stipulated that the terms and conditions of the insurance policy would apply only on payment of the insurance premium. It is only on the date on which the insurance premium is paid or, in terms of the facility extended by the Insurance Corporation of Sri Lanka, the first installment, of the insurance premium payable in four installments, is actually paid, can the assessee claim that the liability to pay the insurance premium had arisen. As, admittedly, no amount was paid towards insurance premium, in the previous year 01.07.1982 to 30.06.1983 (as is evident from the letter of the Insurance Corporation of Sri Lanka dated 30.06.1983), the liability towards the insurance policy did not arise in the previous year 01.07.1982 to 30.06.1983, since the basic condition, relating to actual payment of insurance premium, had not been fulfilled by the assessee by then. This question is also answered in the negative, in favour of the Revenue and against the assessee. QUESTION No.5:

The assessee entered into an agreement, with M/s.Annapoorna Agencies, on 18.08.1981 for procuring purchase orders. Clause (1) of the agreement provided that the agent would be allowed 5% commission on the total value of the order. Clause (5) stipulated that payment of commission shall be made pro-rata to the payments received by the assessee. On the ground that the total work order procured was Rs.4,54,72,289/-, the commission payable was computed at 5% thereof i.e Rs.22,73,614/-; and, as the assessee had received payment of only Rs.95,47,220/- on which the commission payable was Rs.4,77,361/-, the balance commission payable, to the extent of Rs.17.96,253/-, was debited to the account by making a provision.

The Income-tax Officer held that the liability to pay commission arose only on receipt of payments; and, therefore, this provision was to be added back. In appeal, the CIT (Appeals) confirmed this disallowance relying on clause (5) of the agreement. In further appeal, the Tribunal held that it was not in dispute that the contract having been procured, and the service having already been performed, the agent had a right to receive the commission under clause (1) of the agreement, even though payment was to be made pro-rata according to the amounts received by the assessee. The Tribunal upheld the claim of the assessee that the provision, for the balance amount due, was allowable as an accrued liability.

Sri J.V. Prasad, Learned Senior Standing Counsel for Income-Tax, would submit that, as per Clause (5) of the agreement between the parties, commission is to be paid at the rate of 5% of the payment received by the assessee; Clause (1) only speaks of the percentage of commission to be paid on the total value of the purchase; all the terms of the agreement should be read together; if so read, it would be clear that the liability of the assessee, to pay commission, would have accrued or arisen only at the stage when the purchase price is received by the assessee.

On the other hand Sri S. Ravi, Learned Senior Counsel, would submit that, as per the Agreement dated 18.08.1981, M/s. Annapurna Agencies was entitled for 5% commission upon procurement of purchase orders; the Purchase Order was received at the instance of Annapurna Agencies and, therefore, it became entitled to 5% Commission i.e., Rs.22,73,614/-; the Agreement specified that commission shall be paid pro-rata on the payments received by the assessee; as per Clause No.1, the Agent becomes entitled for commission on the total value of the order; Clause No.5 provides for the mode and method of payment; the Tribunal, rightly, concluded that the moment the Purchase Order was secured, in terms of Clause No.1, Annapurna Agencies was entitled for 5% commission; the said commission was accrued liability in the hands of the assessee; and hence they were entitled for deduction.

As is evident from the assessment order, the agreement between the assessee and M/s.Annapoorna Agencies stipulated, in clause (1) thereof, that the agent will be allowed 5% commission on the total value of the order. Clause (5) of the agreement stipulated that this payment of commission shall be made pro-rata to the payments received by the assessee.

The assessee entered into an agency agreement with M/s. Annapurna Agencies, and Clause(1) of the said agreement stipulated that the agent (Annapurna Agencies) would be allowed 5% commission on the total value of the order. Clause (5) of the said agreement stipulated that payment of commission shall be made pro-rata for the payments received by the assessee. As against the total order procured by M/s. Annapurna Agencies for Rs.4,54,72,289, the assessee received payment of only Rs.95,45,220/- during the previous year 01.07.1982 to 30.06.1983. As against its claim for deduction towards commission payable at 5% on the entire value of the order i.e., R.s.22,73,614/-, the assessing authority had allowed deduction of only 5% of the amount received by the assessee i.e for Rs.4,77,361/-, and disallowed the balance Rs.17,96,253/-, on the ground that the liability to pay commission at 5% arose only on receipt of payment by the assessee; and, since the assessee did not receive payment, corresponding to the commission of Rs.17,96,253, it could not be said that a legal liability has arisen in this regard.

As noted hereinabove, Clause (1) of the agreement stipulated that the agent would be allowed 5% commission on the total value of the order. The fact that the agent had discharged its obligation, by procuring orders worth Rs.4,54,72,289/- during the previous year 01.07.1982 to 30.06.1983, is not in dispute. The agreement, therefore, obligated the assessee to allow 5% commission to its agent M/s. Annapurna Agencies. It is no doubt true that Clause (5) stipulated that the actual payment of commission will be made pro-rata to the payment received by the assessee. While the liability arose when the agent procure the order itself, the obligation to make payment was made conditional on the assessee receiving payment from the client, pursuant to the order procured by the agent and after supplies were effected by the assessee.

The obligation to pay commission, in terms of Clause(1) of the agreement, is on the procurement of an order by the agent, and the agent had procured the order during the previous year 01.07.1982 to 30.06.1983. Notwithstanding the fact that the obligation to make payment of commission was dependent on receipt of payment from the client, the liability to pay commission arose on the date on which the order was procured by the agent. The view taken by the Tribunal, that the liability arose, on the date on which the order was procured by M/s. Annapurna Agencies, is a possible view. Even if the view taken by the revenue is presumed also to be a possible view, it cannot be overlooked that, even if two views are possible, the view which is favourable to the assessee must be accepted while construing the provisions of a taxing statute. (Bihar SEB v. Usha Martin Industries ; Mauri Yeast India (P) Ltd. v. State of U.P ; CIT v. Kulu Valley Transport Co. (P) Ltd., ; CCE v. Parle Exports (P) Ltd.,). This question is answered in the affirmative, in favour of the assessee and against the revenue.

In conclusion question Nos.1, 3 and 4 are answered in the negative, in favour of the Revenue and against the assessee, and question Nos.2, 5 and 6 are answered in the affirmative, in favour of the assesssee and against the Revenue. Let the reference be answered accordingly.

______________________________ (RAMESH RANGANATHAN, ACJ)

______________________________ (GUDISEVA SHYAM PRASAD, J)

Date: 01-05-2018.