

**(1978) 01 CAL CK 0030**

**Calcutta High Court**

**Case No:** Income-tax Reference No. 80 of 1975

Commissioner of Income Tax

APPELLANT

Vs

Rajasthan Investment Co. (P.)  
Ltd.

RESPONDENT

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**Date of Decision:** Jan. 13, 1978

**Acts Referred:**

- Income Tax Act, 1961 - Section 145

**Citation:** (1978) 113 ITR 294

**Hon'ble Judges:** Dipak Kumar Sen, J; C.K. Banerji, J

**Bench:** Division Bench

**Advocate:** B.K. Bagchi and B.K. Naha, for the Appellant; None, for the Respondent

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### **Judgement**

Dipak Kumar Sen, J.

This reference arises out of the Income Tax assessment of Messrs. Rajasthan Investment Co. Private Ltd., the assessee, for the assessment years 1968-69, 1969-70, 1970-71 and 1971-72, the relevant previous years ending on the 30th April of 1967, 1968, 1969 and 1970, respectively.

2. The facts found and/or admitted in these proceedings are shortly as follows:

The assessee is an investment company and its source of income is interest received from loans and advances. Its period of account ends on the 30th April each year.

3. The assessee used to maintain its accounts on the mercantile basis. By a resolution of the board of directors of the assessee passed on the 17th March, 1966, it was resolved that with effect from the then current accounting year, i.e., the 1st May, 1966, the assessee would change its method of accounting from mercantile basis to cash basis and this new method should thereafter be regularly followed from year to year.

4. As a result of this change from the 1st May, 1967, onwards the assessee brought into its account whatever interest it actually received and not what was receivable.
5. During the assessment years involved the assessee was entitled to receive interest on loans advanced only from two parties, viz., Messrs, Surajmal Nagarmal and one B. L. Bagla.
6. The Income Tax Officer took note of the fact that Messrs. Surajmal Nagarmal controlled the assessee and that the said firm was regularly crediting the assessee in its account with interest and claiming deductions therefore and concluded that the change of the method of accounting of the assessee was intended only to avoid taxes. Accordingly, the Income Tax Officer added to the income of the assessee all interest receivable by it in all the said years.
7. Being aggrieved, the assessee appealed to the Appellate Assistant Commissioner, who concurred with the decision of the Income Tax Officer in the appeals relating to the first three assessment years and confirmed the addition; but in the appeal relating to the assessment year 1971-72 the Appellate Assistant Commissioner, following the decisions of the Tribunal in other cases, accepted the contentions of the assessee and held that the change-over to the cash system of accounting by the assessee was acceptable and what was actually received as interest should be taxed.
8. From the aforesaid orders of the Appellate Assistant Commissioner, there was one appeal by the revenue and three appeals by the assessee. The Tribunal disposed of all the appeals by its consolidated order passed on the 22nd February, 1974.
9. At the hearing before the Tribunal copies of the books of account of the assessee were submitted and it was found that so far as B.L. Bagla was concerned there had been no payment of interest whatsoever since 1961 and that the entire dues of B. L. Bagla ultimately had to be written off at the end of the accounting year 1972. It was found further that since 1961, payments received by the assessee from Messrs. Surajmal Nagarmal had been next to nothing and that during the four assessment years there were only two payments, viz., a sum of Rs. 1,000 paid in 1968-69 and a sum of Rs. 5,000 paid in 1970-71. It was contended on behalf of the assessee that the assessee was compelled to pay tax on amounts which it had not received and was not likely to receive and, therefore, the directors of the assessee resolved to change the method of accounting so that the true and correct state of affairs would be reflected in the accounts.
10. The contentions of the revenue before the Tribunal were that the debtor, viz., Messrs. Surajmal Nagarmal, was enjoying deductions by crediting its accounts and that the object of the change of method of accounting was to avoid payment of proper tax and, therefore, the same should not be accepted. ,

11. The Tribunal held that there was nothing to show that the change effected by the assessee in its method of accounting was not in good faith and that the propriety of the change adopted by the assessee had to be determined with reference to the assessee's own accounts and not the accounts of its debtors. The Tribunal found that the change-over to the cash basis was more realistic and did not involve any mala fides on the part of the assessee. Accordingly, the Tribunal allowed the appeals of the assessee and dismissed the appeal of the revenue.

12. From this order of the Tribunal at the instance of the Commissioner of Income Tax, West Bengal V, Calcutta, the following questions have been referred to us.

" (1) Whether, on the facts and in the circumstances of the case, and in view of the fact that Messrs. Surajmal Nagarmal was controlling the assessee's business, the Tribunal's Finding that the change in the method of accounting of the assessee from mercantile system to cash system was legally based on reasons ?

(2) Whether, on the facts and in the circumstances of the case, the Tribunal was right in holding that the amount of interest received from Messrs. Surajmal Nagarmal in respect of loan advanced to the said firm by the assessee is not includible in the assessment years 1968-69, 1969-70 and 1970-71 and whether the Tribunal was right in law in holding that: the amount receivable from Surajmal Nagarmal and Sri B. L. Bagla in respect of loans advanced to them by the assessee is not includible for the assessment year 1971-72 ?"

13. None appeared at the hearing on behalf of the assessee. Mr. Bagchi, learned advocate for the revenue, contended that it had been found as a fact by the Income Tax Officer that Messrs. Surajmal Nagarmal controlled the assessee and this was unchallenged and uncontroverted. The Tribunal not having come to any contrary finding, its conclusion that the assessee had changed its method of accounting bona fide could not be accepted.

14. In support of his contentions Mr. Bagchi cited [SHIV PRASAD RAM SAHAI Vs. COMMISSIONER OF Income Tax, UTTAR PRADESH.](#) . The facts in that case were that the assessee, a firm carrying on money-lending business, had shown interest received from its debtors on the basis of mercantile system of accounting throughout for the assessment years 1948-49 to 1956-57 but in the next assessment year, i.e., 1957-58, the accrued interest was not included in its income on the ground that the debtor-firm was in an embarrassed financial position. The Tribunal having held that the said sum should be added to the income of the assessee, the matter came up to the Allahabad High Court. The High Court observed as follows (page 130):

"..... ..once the assessee has adopted the mercantile system of accounting, there is no alternative for the Income Tax Officer but to compute the assessee's income on that system, i.e., on the accrual and not the receipt basis. The choice is entirely that of the assessee. He may even choose to adopt the mercantile system for certain

transactions and the cash basis for other transactions, but once having chosen and regularly employed that system, it is not open to him unilaterally at any time during an accounting year to say that he will not now follow that system in respect of a particular transaction."

15. and upheld the order of the Tribunal.

16. Mr. Bagchi also cited [NEW VICTORIA MILLS CO. LTD Vs. COMMISSIONER OF Income Tax, U. P.](#), . The facts here were that the assessee, a limited company, had claimed deduction of bonus on the basis of actual payment throughout from 1943 to 1947. For the assessment year 1949-50, the previous year ending on the 31st December, 1948, the assessee claimed deduction for provision for bonus which was paid not in the relevant previous year but in the following year. At all stages from the Income Tax Officer up to the Tribunal this claim for deduction was disallowed. On a reference to the Allahabad High Court, the contentions of the revenue were upheld. The High Court observed at page 397 of the report as follows :

" It is no doubt open to the assessee to change his method of accounting but the change should be bona fide and not a casual departure from the regular method which has hitherto been accepted by him for a number of years. Merely because in the subsequent assessment year there was a loss and the bonus actually paid in that year could not be effectively set off but had to be carried forward would furnish no justification for permitting a change in the method of accounting. The bona fides, in the instant case, are absent and the Income Tax Officer was justified in resisting the attempt of the assessee to change its method of accounting."

17. In our opinion none of the above decisions advance the contentions of Mr. Bagchi, The facts in the case of [SHIV PRASAD RAM SAHAI Vs. COMMISSIONER OF Income Tax, UTTAR PRADESH.](#), are entirely different from the facts before us. In that case, there was no general change in the method of accounting but one particular item was sought to be accounted for on an accrual basis for the first time during the accounting year.

18. The case of [NEW VICTORIA MILLS CO. LTD Vs. COMMISSIONER OF Income Tax, U. P.](#), is definitely against the revenue. In the instant case, the Tribunal has accepted the change of method of accounting as bona fide which finding has not been challenged as perverse. Therefore, it is not open to the revenue to agitate the question of bona fides any further.

19. Mr. Bagchi faintly sought to argue that in the instant case the interest receivable should have been taxed u/s 5 of the Income Tax Act, 1961. In support of his contentions Mr. Bagchi cited a decision of the Supreme Court in the case of [The Commissioner of Income Tax, Madras Vs. A. Krishnaswami Mudaliar and Others](#), , where the Supreme Court laid down that whatever be the method of book keeping, in computing the profits of the year, the stock-in-trade must be taken into account.

20. This decision appears to be of little relevance in the facts of the instant case. Mr. Bagchi could not cite any authority for the proposition that even where a cash system of account is followed, Section 5 of the Act could be applied and any item brought to tax on accrual basis. In any event this new case was never agitated at any earlier stage and on the authority of the Supreme Court in [Commissioner of Income Tax, Bihar and Orissa Vs. Kirkend Coal Co.,](#) , we do not feel inclined to go further into this new case.

21. Mr. Bagchi also cited another decision of the Supreme Court in [Keshav Mills Ltd. Vs. Commissioner of Income Tax, Bombay,](#) . The assessee in that case was a non-resident company. The, Supreme Court observed , that while in the case of a resident, mercantile system of accounting regularly adopted is obligatory on the Income Tax authorities for computation of his income, it is doubtful whether that position would be available to a non-resident who maintains his books of account outside British India. This case is, therefore, also of no assistance to the revenue.

22. In our view, the matter has been concluded by the finding of the Tribunal that the change of method of accounting of the assessee was done bona fide and in consonance with the real state of affairs of its business. Accordingly, we answer question No. 1 in the affirmative and in favour of the assessee. As regards question No. 2, it does not appear that the Tribunal has found that any amount received by the assessee from Messrs. Surajmal Nagarmal as interest was not includible in its assessment and, therefore, the first part of the question does not call for any answer. The second part of the question is answered in the affirmative and in favour of the assessee.

Banerji, J.

23. I agree.