(1991) 03 BOM CK 0084

Bombay High Court

Case No: Income-tax Reference No. 279 of 1977

Commissioner of Income Tax	APPELLANT
Vs	
West Coast Paper Mills Ltd.	RESPONDENT

Date of Decision: March 27, 1991

Acts Referred:

- Income Tax Act, 1961 - Section 37(3), 37(4), 80

Citation: (1992) 102 CTR 127 : (1992) 193 ITR 349 : (1992) 1 MhLj 764

Hon'ble Judges: T.D. Sugla, J; B.N. Srikrishna, J

Bench: Division Bench

Advocate: Dr. V. Balasubramanian, for the Appellant; S.J. Mehta, for the Respondent

Judgement

T.D. Sugla, J.
In this reference relating to the assessee''s assessment for the assessment year 1971-72, the Tribunal has referred to this court the following questions of law u/s 256(1) of the Income Tax Act, 1961 :

2. At the instance of the Commissioner :

"Whether, on the facts and in the circumstances of the case and in law, the Tribunal was justified in holding that the assessee was entitled to the deduction of both the amounts of Rs. 12,84,200 and Rs. 14,39,543, respectively, being the actual payment of bonus and the provision for the payment of bonus during the previous year ?"

"Whether, on the facts and in the circumstances of the case and in law, the Tribunal was justified in holding that the following amounts were part of the profit attributable to its priority industry for the purpose of deduction u/s 80-I of the Income Tax Act, 1961 :

(i) Rs. 3,50,000, being the technical collaboration fees received from Messrs. Andhra Pradesh Paper Mills as part of the consideration for the technical know-how supplied by the former to the latter;

(ii) Rs. 4,26,907, being the interest;

(iii) Rs. 2,67,978, being the rent received ?" At the instance of the assessee :

"Whether, on the facts and in the circumstances of the case, the claim of the applicant for deduction of expenses incurred on maintenance of rest houses for employees of the applicant has been rightly disallowed u/s 37(3) up to February 28, 1970, and u/s 37(4) up to March 30, 1970 ?"

3. The assessee is a company. It carries on business in the manufacture and sale of paper. The proceedings relate to the assessment year 1971-72. The assessee, inter alia, claimed deduction of Rs. 47,275 being the amount spent on the maintenance of two rest houses, one at the factory site, that is, Dandeli, and the other at Bangalore. The assessee''s factory is at Dandeli Relying on the provisions of section 37(3) and 37(4) of the Income Tax Act, 1961, the Income Tax Officer disallowed the claim for deduction on revenue account on the ground that no register was kept to show as to who enjoyed the guest house facility.

4. The assessee was a priority industry and was, as such, entitled to deduction u/s 80-I of the Income Tax Act, 1961. It claimed that the sums of Rs. 3,50,000 being technical collaboration fee received by it from Messrs. Andhra Pradesh Paper Mills, Rs. 4,26,907 being interest on short-term deposits and Rs. 2,67,978 being rent received represented its profits and gains attributable to the priority industry. However, the Income Tax Officer held that these amounts were not attributable to the priority industry and excluded them from the profits of the priority industry, thereby reducing the deduction allowable to the assessee u/s 80-I.

5. It is common ground that, with the introduction of the Payment of Bonus Act, 1965, payment of bonus to employees became the assessee''s statutory obligation. However, even though the assessee was following the mercantile system of accounting in respect of other income and expenditure, it continued to follow the cash method of accountancy with regard to bonus liability. During the previous year relevant for the year under reference, the assessee paid bonus of Rs. 12,84,200 and claimed it as a revenue deduction which the Income Tax Officer allowed. The assessee, however, further claimed deduction of Rs. 14,39,453 being provision for bonus on the ground that, during the previous year, the assessee had received a communication dated October 15, 1969, from the Federation of Indian Chambers of Commerce and Industry, communicating the opinion of the Company Law Board that provision for bonus should be made in the accounts of the year for which the bonus was payable. However, the Income Tax Officer rejected this contention stating that since the assessee was following the cash method in regard to bonus payment, it could not be permitted to change its method.

6. On appeal, the assessee''s claim in regard to the expenditure of Rs. 47,275 on the maintenance of two rest houses was rejected both by the Appellate Assistant Commissioner and the Tribunal mainly on the ground that the claim was hit by the

provisions of section 37(3) and 37(4) as the assessee had not maintained a register to show as to who enjoyed the guest house facility. The claim that the three items of income which the Income Tax Officer had considered as not attributed to the priority industry was accepted by the Appellate Assistant Commissioner and the departmental appeal there against was rejected by the Tribunal following its order in the assessee''s own case for the earlier years.

7. As regards the claim for bonus, the Appellate Assistant Commissioner, relying on the Supreme Court decision in the case of The Kedarnath Jute Mfg. Co. Ltd. Vs. The Commissioner of Income Tax, (Central), Calcutta, , held that the provision for bonus of Rs. 14,39,453 was allowable as deduction. However, for reasons stated of him in the order, he directed that the deduction of smaller amount of Rs. 12,84,200 on cash basis could not, at the same time, be allowed. Accordingly, he directed the withdrawal of the deduction of amount. The Tribunal has considered this issue in its order at length. It was come to the conclusion that the Appellate Assistant Commissioner was not right in withdrawing the deduction of the sum of Rs. 12,84,200 which was allowed by the Income Tax Officer.

8. So far as the second question referred to us at the instance of the Commissioner is concerned, counsel are agreed that the issue is covered by our court''s decision in the assessee''s own case in Commissioner of Income Tax Vs. West Coast Paper Mills Ltd., . Accordingly, we answer the second question in the affirmative and in favour of the assessee.

9. As regards the only question referred to us at the instance of the assessee, we find ourselves in agreement with the departmental authorities and the Tribunal that the distinction drawn by the assessee between "rest house" and "guest house" is to be scared only to be rejected. If at all there is a distinction, it is a distinction without any substance. That being so, it cannot perhaps be disputed that up to a particular date, the provisions of section 37(3) are attracted in terms of which expenditure on the maintenance of a guest house can be allowed only if a register is maintained. The register having admittedly not been maintained, the expenditure could not have been allowed. After that date, the provisions of section 37(4) are applicable which completely prohibit allowance of any deduction of expenditure on maintenance of guest house. Having regard to the above discussion, so far as the question at the instance of the assessee is concerned, we answer the question in the affirmative and in favour of the Revenue.

10. This takes us to the first question referred to us at the instance of the Commissioner. The relevant facts have already been stated by us to the earlier paragraphs. In this context, it may be desirable to refer to the provisions of section 145 which read as under :

"Section 145(1) : Income chargeable under the head ''Profits 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 :

Provided that in case where the accounts are correct and complete to the satisfaction of the Assessing Officer but the method employed is such that, in the opinion of the Assessing Officer, the income cannot properly be deducted therefrom, then the computation shall be made upon such basis and in such manner as the Assessing Officer may determine :

Provided further that where no method of accounting is regularly employed by the assessee, any income by way of interest on securities shall be chargeable to tax as the income of the previous year in which such interest is due to the assessee :

Provided also that nothing contained in this sub-section shall preclude an assessee from being charged to Income Tax in respect of any interest on securities received by him in a previous year if such interest had not been charged to Income Tax for any earlier previous year."

11. Evidently, the income, profits and gains of business or profession are to be computed in accordance with the method of accounting regularly employed by the assessee. It is only in cases where, from the method of accounting regularly employed, it is not possible to deduce the income correctly that the Income Tax Officer can compute the income on such basis and in such manner as he may determine. There is no dispute that the assessee was maintaining its books in so far as bonus is concerned on the cash basis. There cannot also possibly be any dispute that, during the previous year, the assessee changed its method on the basis of a communication received from the Federation of Indian Chambers of Commerce and Industry communicating the opinion of the Company Law Board. In the circumstances, it may not be possible to hold and in fact it has not been held by the departmental authorities that the change of method in this regard claimed by the assessee is not bona fide. It is not as if an assessee can never change its method of accounting. The method of accounting can be changed bona fide. If the method is followed regularly and is bona fide there is not appear to be any reason why the change should not be allowed. Dr. Balasubramanian, it may be stated, had contended that the assessee could not change the method of accounting without seeking the permission of the Income Tax Officer and that it will be for the Income Tax Officer to impose conditions for allowing the change of method. However, he was not able to point out any authority in support of his submission. Accordingly, we proceed to examine the issue on the basis that the change of method in this case as regards bonus has been bona fide and has been consistently and regularly followed thereafter by the assessee.

12. The question that requires consideration is only this because of the change in the method of accounting during the year under reference, the assessee is claiming deduction in respect of bonus liability both on cash basis and on mercantile basis. The question is whether the assessee can do it. Here again, in our judgment,

whenever there is a change of method, something of this kind is bound to happen in the year of change of method. In case the assessee had changed its method from mercantile system to cash system, it might have been that in the year of change, no deduction what so ever could have been claimed or allowed. However, that will be no reason for not allowing the claim on the basis of the changed method so far as the change is concerned or on the earlier method if the liability in regard thereto has not already been allowed as deduction. Accordingly, we are in agreement with the Tribunal that the assessee was entitled to the deduction for this year both as regards the provision for bonus as also the bonus actually paid during the previous year. The first question referred to us at the instance of the Commissioner is, therefore, answered in the affirmative and in favour of the assessee.

13. There will be no order as to costs.