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ALLIED MOTORS (P) LTD.

v.

COMMISSIONER OF INCOME TAX, DELHI

MARCH 10, 1997

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[A.M. AHMADI, CJ., SUJATA V. MANOHAR
AND K. VENKATASWAMI, JJ.]

Income Tax Act, 1961 :

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Section 43-B first proviso—Retrospective operation of—Held : First proviso effective since inception of S. 43-B—Nature and object of proviso considered—Reasonable construction applied—Memorandum of Reasons of Finance Bill, 1989 and Departmental Circular No. 550 dated 1-1-1990, considered—Interpretation of Statutes.

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Section 43-B first proviso—Nature and object of—Held : Remedial in nature, designed to eliminate unintended consequences of S. 43-B which might cause undue hardship to the assessee in a specific situation and thereby make the provision unworkable or unjust—Memorandum explaining provisions in Finance Bill of 1983 and Budget Speech of Finance Minister for 1983-84, considered.

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The petitioner-assessee filed an Income Tax Return for the Assessment Year 1984-85 in which the assessee had claimed a deduction on account of sales tax collected by the assessee for the last quarter of the relevant previous year. The Income Tax Officer under Section 43-B of the Income Tax Act, 1961 disallowed the deduction, which was claimed by the assessee. Section 43-B was inserted in the Act with effect from 1-4-1984. This Section as it originally, stood, did not contain the first proviso. This proviso was inserted by the Finance Act of 1987, which came into effect from 1-4-1988. Explanation 2 was added to Section 43-B by the Finance Act of 1989 with retrospective effect from 1-4-1984. These provisions were explained in the Memorandum of the Finance Bill of 1983 and the Budget Speech of the Finance Minister for the year 1983-84. The appeal filed by the assessee before the Income Tax Appellate Tribunal was dismissed. Hence this appeal.

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On behalf of the petitioner, it was contended that the first proviso

which was inserted by the amending Finance Act of 1987 should be given retrospective effect and be read as forming a part of Section 43-B from its inception. A

Allowing the appeal, this Court

HELD : 1. In view of the Memorandum explaining the provisions of Section 43-B of the Income Tax Act, 1961 in the Finance Bill of 1983 and the Budget Speech of the Finance Minister for the year 1983-84, it is clear that Section 43-B aimed at the curbing the activities of those tax payers who did not discharge their statutory liability of payment of excise duty, employer's contribution to provident fund etc. for long periods of time but claimed deductions in that regard from their income on the ground that the liability to pay these amounts had been incurred by them in the relevant previous year. It was not realised that the language in which Section 43-B was worded would cause hardship to those tax payers who had paid sales-tax within the statutory period prescribed for this payment, although the payment so made by them did not fall in the relevant previous year. Hence, the first proviso was inserted in Section 43-B. The amendment which was made by the Finance Act of 1987 in Section 43-B by inserting, *inter alia*, the first proviso, was remedial in nature, designed to eliminate unintended consequences which may cause undue hardship to the assessee and which made the provision unworkable or unjust in a specific situation. B
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[786-B, H, 787-A-E]

2. Explanation 2 was added to Section 43-B of the Act by the Finance Act of 1989 with retrospective effect from 1-4-1984. The Memorandum of Reasons for the Finance Act, 1989 proceeds on the basis that Section 43-B read with the proviso takes care of the hardship situation and hence Explanation 2 can be inserted with retrospective effect to make clear the ambit of Section 43-B(a). Therefore, Section 43-B(a), the first proviso to Section 43-B and Explanation 2 have to be read together as giving effect to the true intention of Section 43-B. If Explanation is retrospective, the first proviso will have to be so construed. Read in this light also, the proviso has to be read into Section 43-B from its inception along with Explanation 2. [788-B, 789-B-E] F
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3. The Departmental Circular No. 550 dated 1-1-1990 shows that the departmental understanding also is that Section 43-B, the proviso and Explanation 2 have to be read together as expressing the true intention of H

- A Section 43-B. Explanation 2 has been expressly made retrospective. The first proviso, however, cannot be isolated from Explanation 2 and the main body of Section 43-B. Without the first proviso, Explanation 2 would not obviate the hardship or the unintended consequences of Section 43-B. The proviso supplies an obvious omission. But for this proviso the ambit of Section 43-B becomes unduly wide bringing within its scope these payments, which were not intended to be prohibited from the category of permissible deductions. [790-F-G]

Goodyear India Ltd. v. State of Haryana & Anr., 188 ITR 402 and *R.B. Jodha Mal Kuthiala v. CIT*, 82 ITR 570, relied on.

- C *CIT v. Chandulal Venichand*, (1994) 209 ITR 7 (Guj.), *CIT v. Sri Jagannath Steel Corporation*, (1991) 191 ITR 676 (Cal.) and *Jamshedpur Motor Accessories Stores v. Union of India & Ors.*, (1991) 189 ITR 70 (Pat.), approved.

- D *Escorts Ltd. v. Union of India*, 189 ITR 81 (Del.) and *Sanghi Motors v. Union of India*, 187 ITR 703 (Del.), overruled.

G.P. Singh : "*Principles of Statutory Interpretation*", 4th Edn., p. 291, referred to.

- E CIVIL APPELLATE JURISDICTION : Tax Reference No. 2 of 1993 Etc.

From the Order dated 3.3.88 of the Commissioner of Income Tax (Appeals) VIII, New Delhi in A.No. 171 of 1987-88.

- F C.S. Agarwal, B.V. Desai, P.K. Malik and Ms. Shashi Soharu for the Petitioner in T.R. No. 2/93.

Ms. Geetanjali Mohan for the appellant in C.A. No. 3175/91.

- G M.S. Syali and Ms. Geetanjali Mohan for the Appellant in C.A. No. 2380/91.

A. Raghuvir, (Ms. Lakshmi Iyengar) for B.K. Prasad for the Respondent and Petitioner in T.R. No. 2/93 and T.R. No. 1/94.

- H The Judgment of the Court was delivered by

MRS. SUJATA V. MANOHAR, J. The two Income-tax References which are before us deal with a common question relating to the interpretation of Section 43B of the Income-tax Act, 1961. The references have been made under Section 256(1) of the Income-tax Act, 1961. Since the same question arises in the two civil appeals also these appeals have been heard along with these references. For the sake of convenience, we are taking the statement of the case in Income-tax Reference No. 2 of 1993.

The following question has been referred to us under Section 256(1):-

"Whether on the facts and in the circumstances of the case, the sales-tax collected by the assessee and paid after the end of the relevant previous year but within the time allowed under the relevant sales-tax law is to be disallowed under Section 43B of the Income-tax Act, 1961 while computing the business income of the said previous year?"

The relevant assessment year is 1984-85, the relevant accounting period being the year ending on 30th of June, 1983. The assessee filed the return declaring an income of Rs. 1,91,940. The Income-tax Officer, however, disallowed, *inter alia*, deduction claimed by the assessee of an amount of Rs. 5,78,240 which was on account of sales-tax collected by the assessee for the last quarter of the relevant accounting year. This amount was payable within 30 days of the end of the quarter. The deduction which was claimed by the assessee was disallowed by the Income-tax Officer under Section 43B of the Income-tax Act, 1961 which was inserted in the statute with effect from 1.4.1984. The assessee filed an appeal before the Commissioner of Income-tax (Appeals), *inter alia*, in respect of this disallowance. However, the appeal was dismissed. The assessee filed an appeal before the Income-tax Appellate Tribunal. The tribunal also dismissed the appeal on the basis of the judgments of the Delhi High Court in the case of *Sanghi Motors v. Union of India*, (187 ITR 703) and *Escorts Ltd. v. Union of India & Ors.*, (189 ITR 81). Hence the present reference has come before us. One of the judgments relied upon by the tribunal was the judgment in the case of *Escorts Ltd. v. Union of India*, (supra). Civil Appeal No. 3175 (NT) of 1991 is an appeal from the decision of the Delhi High Court in the above case which is being heard along with the present tax-references.

The relevant provisions of Section 43B for our purposes are as

A follows :-

"43B :- *Certain deductions to be only on actual payment --*

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Notwithstanding anything contained in any other provision of this Act, a deduction otherwise allowable under this Act in respect of --

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(a) any sum payable by the assessee by way of tax, duty, cess or fee, by whatever name called, under any law for the time being in force, or

(b)

(c)

(d)

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shall be allowed (irrespective of the previous year in which the liability to pay such sum was incurred by the assessee according to the method of accounting regularly employed by him) only in computing the income referred to in section 28 of that previous year in which such sum is actually paid by him :

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*Provided that nothing contained in this section shall apply in relation to any sum referred to in clause (a) or clause (c) or clause (d) which is actually paid by the assessee on or before the due date applicable in his case for furnishing the return of income under sub-section (1) of section 139 in respect of the previous year in which the liability to pay such sum was incurred as aforesaid and the evidence of such payment is furnished by the assessee along with the such return :

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Provided further

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Explanation 1 -

**Explanation 2 -- For the purposes of clause (a), as in force at all material times, 'any sum payable means a sum for which the assessee incurred liability in the previous year even though such sum might not have been payable within that year under the relevant law.

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Explanation 3 -

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Explanation 4 -

Section 43B was inserted in the Income-tax Act, 1961 with effect from 1.4.1984. The section, as it originally stood, did not contain the two provisos. The first proviso has been set out above. This proviso was inserted by the Finance Act of 1987 which came into effect from 1.4.1988. Explanation 2 has been added subsequently by the Finance Act of 1989 but with retrospective effect from 1.4.1984. In these References and appeals we are concerned with the application of Section 43B as it stood before the provisos were added.

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Prior to the insertion of Section 43B in the Income-tax Act, 1961, income chargeable under the head 'profits and gains' of business or profession was computable in accordance with the method of accounting regularly employed by the assessee as per Section 145 of the Income-tax Act, 1961. An assessee who had adopted the mercantile system of accounting would be entitled to account for his income and expenditure on the basis of accrual and not on the basis of actual receipt or disbursement. After insertion of Section 43B, however, even if the assessee had regularly adopted mercantile system of accounting, the amount of tax payable by the assessee could be deducted only in the year in which the sum was actually paid and not in the year in which the assessee incurred the liability to pay that tax. Hence an assessee (as in the present case), who had collected sales-tax in the last quarter of the previous accounting year and deposited it in the treasury within the statutory period falling in the next accounting year, would not be entitled to claim any deduction for it. The sales-tax so collected will form a part of the assessee's income. To obviate this kind of unexpected outcome of Section 43B, the first proviso was added in Section 43B by the Finance Act of 1987. The proviso makes it clear that the Section will not apply in relation to any sum which is actually paid by the assessee in the next accounting year if it is paid on or before the due date for furnishing the return of income in respect of the previous year in which the liability to pay such sum was incurred and the evidence of such payment is furnished by the assessee along with the return.

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The proviso, however, was not on the statute book when the assessments were made in respect of these assesseees since the assessments pertain to assessment years prior to the insertion of the proviso in Section

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A 43B. The assessee, however, contend that the proviso should be given effect to retrospectively from the date when Section 43B became a part of the Income-tax Act, 1961, as it is intended to obviate unexpected hardships in the application of Section 43B.

B To understand the circumstances in which Section 43B came to be inserted in the Income-tax Act and the mischief which it sought to prevent, it is necessary to look at the memorandum explaining the provisions in the Finance Bill of 1983 [(1983) 140 ITR (St.) 160] :-

C "59. Under the Income-tax Act, profits and gains of business and profession are computed in accordance with the method of accounting regularly employed by the assessee. Broadly stated, under the mercantile system of accounting, income and outgo are accounted for on the basis of accrual and not on the basis of actual disbursements or receipts. For the purposes of computation of profits and gains of business and profession, the Income-tax Act defines the word 'paid' to mean 'actually paid or incurred' according to the method of accounting on the basis of which the profits or gains are computed.

E 60. Several cases have come to notice where tax payers do not discharge their statutory liability such as in respect of excise duty, employer's contribution to provident fund, Employees' State Insurance Scheme, etc. for long period of time, extending sometimes to several years. For the purpose of their income-tax assessments, they claim the liability as deduction on the ground that they maintain accounts on mercantile or accrual basis. On the other hand they dispute the liability and do not discharge the same. For some reason or the other, undisputed liabilities also are not paid.

F To curb this practice, it is proposed to provide that deduction for any sum payable by the assessee by way of tax or duty under any law for the time being in force (irrespective of whether such tax or duty is disputed or not) or any sum payable by the assessee as an employer by way of contribution to any provident fund, or superannuation fund or gratuity fund or any other fund for the welfare of employees shall be allowed only in computing the income of that previous year in which such sum is actually paid by him."

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The Budget Speech of the Finance Minister for the year 1983-84, A reproduced in (1983) 140 ITR (St.) 31, is to the same effect.

Section 43B was, therefore, clearly aimed at curbing the activities of those tax payers who did not discharge their statutory liability of payment of excise duty, employer's contribution to provident fund etc. for long periods of time but claimed deductions in that regard from their income B on the ground that the liability to pay these amounts had been incurred by them in the relevant previous year. It was to stop this mischief that Section 43B was inserted. It was clearly not realised that the language in which Section 43B was worded would cause hardship to those tax payers who had paid sales-tax within the statutory period prescribed for this payment, C although the payment so made by them did not fall in the relevant previous year. This was because the sales-tax collected pertained to the last quarter of the relevant accounting year. It could, be paid only in the next quarter which fell in the next accounting year. Therefore, even when the sales-tax had in fact been paid by the assessee within the statutory period prescribed D for its payment and prior to the filing of the income tax return, these assessees were unwittingly prevented from claiming a legitimate deduction in respect of the tax paid by them. This was not intended by Section 43B. Hence the first proviso was inserted in Section 43B. The amendment which was made by the Finance Act of 1987 in Section 43B by inserting, *inter alia*, E the first proviso, was remedial in nature, designed to eliminate unintended consequences which may cause undue hardship to the assessee and which made the provision unworkable or unjust in a specific situation.

Looking to the curative nature of the amendment made by the Finance Act of 1987 it has been submitted before us that the proviso which F is inserted by the amending Finance Act of 1987 should be given retrospective effect and be read as forming a part of Section 43B from its inception. This submission has taken support from decisions of a number of High Courts before whom this question came up for consideration. The High G Courts of Calcutta, Gujarat, Karnataka, Orissa, Gauhati, Rajasthan, Andhra Pradesh, Patna and Kerala appear to have taken the view that the proviso must be given retrospective effect. Some of these High Courts have held that "sum payable" under Section 43B(a) refers only to the sum payable in the same accounting year, thus excluding sales tax payable in the next accounting year from the ambit of Section 43B(a). The Delhi High H

A Court has taken a contrary view holding that the first proviso to Section 43B operates only prospectively. We will refer only to some of these judgments.

B Explanation 2 was added to Section 43B by the Finance Act of 1989 with retrospective effect from 1.4.1984. The Memorandum explaining the reasons for introducing Explanation 2, states, *inter alia*, as follows [(1989) 176 ITR (St.) 123] :-

C "24. Under the existing provisions of section 43B of the Income-tax Act, a deduction for any sum payable by way of tax, duty, cess or fee, etc., is allowed on actual payment basis only. The objective behind these provisions is to provide for a tax disincentive by denying deduction in respect of a statutory liability which is not paid in time. The Finance Act, 1987, inserted a proviso to section 43B to provide that any sum payable by way of tax or duty, etc., liability for which was incurred in the previous year will be allowed as a deduction, if it is actually paid by the due date of furnishing the return under section 139(1) of the Income-tax Act, in respect of the assessment year to which the aforesaid previous year relates. This proviso was introduced to remove the hardship caused to certain taxpayers who had represented that since the sales tax for the last quarter cannot be paid within that previous year, the original provisions of section 43B will unnecessarily involve disallowance of the payment for the last quarter.

F Certain courts have interpreted the provisions of section 43B in a manner which may negate the very operation of this section. The interpretation given by these courts revolves around the use of the words 'any sum payable'. The interpretation given to these words is that the amount payable in a particular year should also be statutorily payable under the relevant statute in the same year.

G This is against the legislative intent and it is, therefore, proposed, by way of a clarificatory amendment and for removal of doubts, that the words 'any sum payable' be defined to mean any sum, liability for which has been incurred by the taxpayer during the previous year irrespective of the date by which such sum is

H statutorily payable.

This amendment will take effect from April 1, 1984." A

While interpreting Section 43B without the first proviso some of the High Courts, in order to prevent undue hardship to the assessee, had taken the view that Section 43B would not be attracted unless the sum payable by the assessee by way of tax, duty, cess or fee was payable in the same accounting year. If the tax was payable in the next accounting year, Section 43B would not be attracted. This was done in order to prevent any undue hardship to assesseees such as the ones before us. The memorandum of reasons takes note of the combined effect of Section 43B and the first proviso inserted by the Finance Act, 1987. After referring to the fact that the first proviso now removes the hardship caused to such tax payers it explains the insertion of Explanation 2 as being for the purpose of removing any ambiguity about the term 'any sum payable' under clause (a) of Section 43B. This Explanation is made retrospective. The Memorandum seems to proceed on the basis that Section 43B read with the proviso takes care of the hardship situation and hence Explanation 2 can be inserted with retrospective effect to make clear the ambit of Section 43B(a). Therefore, Section 43B(a), the first proviso to Section 43B and Explanation 2 have to be read together as giving effect to the true intention of Section 43B. If Explanation 2 is retrospective, the first proviso will have to be so construed. Read in this light also, the proviso has to be read into Section 43B from its inception along with Explanation 2. B C D E

This position is reinforced by a departmental Circular No. 550 dated 1st of January 1990, [(1990) 182 ITR (St.) 114, 123] :-

"AMENDMENT OF PROVISIONS RELATING TO CERTAIN DEDUCTIONS TO BE ALLOWED ONLY ON ACTUAL PAYMENT: F

15.1 Under the existing provisions of section 43B of the Income-tax Act 1961, a deduction for any sum payable by way of tax, duty cess or fee, etc., is allowed on actual payment basis only. The objective behind these provisions is to provide for a tax disincentive by denying deduction in respect of a 'statutory liability' which is not paid in time. The Finance Act, 1987, inserted a proviso to section 43B to provide that any sum payable by way of tax or duty, etc., liability for which was incurred in the previous year will be G H

A allowed as a deduction, if it is actually paid by the due date of furnishing the return under section 139(1) of the Income-tax Act in respect of the assessment year to which the aforesaid previous year relates. This proviso was introduced to remove the hardship caused to certain taxpayers who had represented that since the sales tax for the last quarter cannot be paid within the previous year, the original provisions of section 43B will unnecessarily involve disallowance of the payment for the last quarter.

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C Certain courts have interpreted the provisions of section 43B in a manner which may negate the very operation of this section. The interpretation given by these courts revolves around the use of the words 'any sum payable'. The interpretation given to these words is that the amount payable in a particular year should also be statutorily payable under the relevant statute in the same year. Thus, the sales tax in respect of sales made in the last quarter was held to be totally outside the purview of section 43B since the same is not statutorily payable in the financial year to which it relates. This is against the legislative intent and, therefore, by way of inserting an Explanation, it has been clarified that the words 'any sum payable' shall mean any sum, liability for which has been incurred by the taxpayer during the previous year irrespective of the date by which such sum is statutorily payable....."

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F The departmental understanding also appears to be that Section 43B, the proviso and Explanation 2 have to be read together as expressing the true intention of Section 43B. Explanation 2 has been expressly made retrospective. The first proviso, however, cannot be isolated from Explanation 2 and the main body of Section 43B. Without the first proviso, Explanation 2 would not obviate the hardship or the unintended consequences of Section 43B. The proviso supplies an obvious omission. But for this proviso the ambit of Section 43B becomes unduly wide bringing within its scope those payments which were not intended to be prohibited from the category of permissible deductions.

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H In the case of *Goodyear India Ltd. v. State of Haryana and Anr.* (188) ITR 402 this Court said that the rule of reasonable construction must be applied while construing a statute. Literal construction should be avoided

if it defeats the manifest object and purpose of the Act.

Therefore, in the well known words of Judge Learned Hand, one cannot make a fortress out of the dictionary; and should remember that statutes have some purpose and object to accomplish whose sympathetic and imaginative discovery is the surest guide to their meaning. In the case of *R.B Jodha Mal Kuthiala v. Commissioner of Income-Tax, Punjab, Jammu & Kashmir and Himachal Pradesh*, (82) ITR 570, this Court said that one should apply the rule of reasonable interpretation. A proviso which is inserted to remedy unintended consequences and to make the provision workable, a proviso which supplies an obvious omission in the section and is required to be read into the section to give the section a reasonable interpretation, requires to be treated as retrospective in operation so that a reasonable interpretation can be given to the section as a whole.

This view has been accepted by a number of High Courts. In the case of *Commissioner of Income-Tax v. Chandulal Venichand*, [1994] 209 ITR 7, the Gujarat High Court has held that the first proviso to Section 43B is retrospective and sales-tax for the last quarter paid before the filing of the return for the assessment year is deductible. This decision deals with assessment year 1984-85. The Calcutta High Court in the case of *Commissioner of Income-Tax v. Sri Jagannath Steel Corporation*, [1991] 191 ITR 676, has taken a similar view holding that the statutory liability for sales-tax actually discharged after the expiry of the accounting year in compliance with the relevant statute is entitled to deduction under Section 43B. The High Court has held the amendment to be clarificatory and, therefore, retrospective. The Gujarat High Court in the above case held the amendment to be curative and explanatory and hence retrospective. The Patna High Court has also held the amendment inserting the first proviso to be explanatory in the case of *Jamshedpur Motor Accessories Stores v. Union of India and Ors.*, [1991] 189 ITR 70. It has held the amendment inserting first proviso to be retrospective. The special leave petition from this decision of the Patna High Court was dismissed. The view of the Delhi High Court, therefore, that the first proviso to Section 43B will be available only prospectively does not appear to be correct. As observed by G.P. Singh in his *Principles of Statutory Interpretation*, 4th Edn. Page 291, "It is well settled that if a statute is curative or merely declaratory of the previous law retrospective operation is generally intended." In fact the amendment

A would not serve its object in such a situation unless it is construed as retrospective. The view, therefore, taken by the Delhi High Court cannot be sustained.

B In the premises the appeals are allowed and the Income-tax references are answered in favour of the assesseees and against the revenue. In the circumstances, however, there will be no order as to costs.

V.S.S.

Appeals allowed.