A COMMISSIONER OF INCOME TAX, CALCUTTA

*v.*

SUGAULI SUGAR WORKS (P) LTD.

FEBRUARY 4, 1999

B [M. SRINIVASAN AND U.C. BANERJEE, JJ.]

*Income Tax Act, 1961 :*

*Section 41—Applicability of—Necessary condition for.*

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*Assessee—Respondent-Private Limited Company—Assessment year 1965-66—Assessment of tax—Assessee transferred a sum of Rs. 3,45,000 out of the suspense account running from 1946-47 to 1948-49 to the capital reserve account—The Income Tax Officer found that an amount of Rs. 1,29,000 was* D *with reference to the deposits and advances which had been paid back and therefore he included a sum of Rs. 2,56,529 under Section 41 of the Income Tax Act in the total income of the assessee—On appeal by assessee Appellate Assistant Commissioner confirmed the Order of I.T.O.—Tribunal held unilateral entry by assessee in the accounts transferring the amount to the capital reserve account would not bring the matter within the scope of Section* E *41—On reference High Court held in favour of assessee—Appeal before Supreme Court—Held view taken by High Court is correct—Section 41 contemplates the obtaining by the assessee of an amount either in cash or in any other manner whatsoever or a benefit by way of remission or cessation and it should be of a particular amount obtained by him—Thus, the obtaining by* F *the assessee of a benefit by virtue of remission or cessation is sine qua non for the application of this Section—The mere fact that the assessee has made an entry of transfer in his accounts unilaterally will not enable the Department to say that Section 41 would apply and the amount should be included in the total income of the assessee—The question whether the liability is actually barred by limitation is not a matter which can be decided by considering the* G *assessee's case alone but it is a matter which has to be decided only if the creditor is before the concerned authority—In the absence of the creditor, it is not possible for the authority to come to a conclusion that the debt is barred and has become unenforceable—There may be circumstances which may enable the creditor to come with a proceeding for enforcement of the debt* H *even after expiry of the normal period of limitation as provided in the*

*Limitation Act.* A

*Commissioner of Income Tax* **v.** *General Industrial Society Ltd.,* **(1994) 207 ITR 169;** *Commissioner of Income-Tax* **v.** *Jiajee Rao Cotton Mills Ltd.,* **(1997) 227 ITR 860, held inapplicable.**

*Commissioner of Income-Tax* **v.** *Bennett Coleman & Co. Ltd.,* **(1993) 201 ITR 1021, disapproved.** B

*The Commissioner of Income-Tax Gujarat II, Ahmedabad* **v.** *M/s. Bharat Iron & Steel Industries, Bhavnagar,* **(1993) Tax LR 188;** *J.K. Chemicals Ltd.* **v.** *Commissioner of Income-Tax, Bombay City II,* **(1966) 62 ITR 34, approved.** C

*Kohinoor Mills Co. Ltd.* **v.** *CIT,* **(1963) 49 ITR 578, referred to.**

*Limitation Act, 1963 :*

*Debt—Recovery of—Period of limitation—Expiry of—Effect—Held does not extinguish the debt—Only prevent the creditor from enforcing the debtor—Mere entry in the books of accounts of the debtor made unilaterally without any act on the part of the creditor will not enable the debtor to say that the liability has come to an end.* D

*Bombay Dyeing & Manufacturing Co. Ltd.* **v.** *The State of Bombay & Ors.,* **[1958] SCR 1122; referred to.** E

CIVIL APPELLATE JURISDICTION : Civil Appeal No. 2344 of 1992.

From the Judgment and Order dated 7.4..81 of the Calcutta High Court in I.T.R. No. 205 of 1976. F

Ranbir Chandra, Rajiv Nanda, P. Parmeswaran and B.K. Prasad, Advs. for the Appellant.

The following Order of the Court was delivered : G

The respondent-assessee is a private limited company. In the proceedings for assessment of tax for the year ending 30.6.1964 relevant to the Assessment year 1965-66, the assessee transferred a sum of Rs. 3,45,000 out of the suspense account running from 1946-47 to 1948-49 to the capital reserve account. The Income Tax Officer found that an amount of Rs. H

A 1,29,.000 was with reference to the deposits and advances which had been paid back and he included a sum of Rs. 2,56,529 under Section 41 of the Income Tax Act in the total income of the assessee. The assessee went on appeal before the Appellate Assistant Commissioner and the order of the I.T.O. was confirmed. The assessee carried the matter to the Tribunal. The Tribunal accepted the contention of the assessee and held that its unilateral B entry in the accounts transferring the amount to the capital reserve account would not bring the matter within the scope of Section 41 of the Income Tax Act and consequently held in favour of the assessee. The decision of the Tribunal was challenged before the High Court. The High Court observed :

> C "The transfer of an entry is a unilateral act of the assessee, who is a debtor to its employees. We fail to see how a debtor, by his own unilateral act, can bring about the cessation or remission of his liability. Revision has to be granted by the creditor. It is not in dispute and it indeed can not be disputed that it is not a case of remission of liability. Similarly a unilateral act on the part of the D debtor cannot bring about a cessation of his liability. The cessation of the liability may occur either by reason of the operation of law, that is, on the liability becoming unenforceable at law by the creditor and the debtor declaring unequivocally his intention not to honour his liability when payment is demanded by the creditor or a contract between the parties, or by discharge of the debt the E debtor making payment thereof to his creditor. Transfer of an entry is neither an agreement between the parties nor payment of the liability."

On that reasoning, the High Court answered the question in reference in favour of the assessee. Aggrieved thereby, the Commissioner of F Income Tax has preferred this appeal.

2. Learned counsel for the appellant contends that in the facts of the present case, the liability has come to an end as a period of more than 20 years had elapsed and the creditor had not taken any step to recover the G amount. Consequently, according to him, there is a cessation of the debt and the matter would fall within the scope of Section 41 of the Act. Section 41 reads as follows :

> "Where an allowance or deduction has been made in the assessment for any year in respect of loss, expenditure or H trading liability incurred by the assessee and subsequently

during any previous year, the assessee has obtained, whether in cash or in any other manner whatsoever, any amount in respect of such loss or expenditure or some benefit in respect of such trading liability by way of remission or cessation thereof, the amount obtained by him, shall be deemed to be profits and gain of business or profession and accordingly chargeable to income tax as the income of that previous year, whether the business or profession in respect of which the allowance or deduction has been made in existence in that year or not."

3. It will be seen that the following words in the Section are important: "the assessee had obtained, whether in cash or in any other manner whatsoever any amount in respect of such loss or expenditure or some benefit in respect of such trading liability by way of remission or cessation thereof, the amount obtained by him". Thus, the section Contemplates the obtaining by the assessee of an amount either in cash or in any other manner whatsoever or a benefit by way of remission or cessation and it should be of a particular amount obtained by him. Thus, the obtaining by the assessee of a benefit by virtue of remission or cessation is *sine qua non* for the application of this Section. The mere fact that the assess has made an entry of transfer in his accounts unilaterally will not enable the Department to say that Section 41 would apply and the amount should be included in the total income of the assessee. The reasoning of the High Court is correct and we are in agreement with the same.

4. Learned counsel for the appellant draws our attention to the judgment of the Calcutta High Court in *Commissioner of Income Tax* v. *General Industrial Society Ltd.,* (1994) 207 ITR 169. The Division Bench of the Calcutta High Court has taken care to set out the two important factors in that case which weighed with them to come to the particular conclusion. The Bench said :

"It appears from the assessment order that there is one peculiar aspect in the present case. It is the practice of the assessee to write back such unclaimed and unspent liabilities from year to year on grounds of bar limitation of the liability and to get away without paying tax on such amount written back to profit on the same plea. This has been happening since the assessment year 1977-78. This fact, to our mind, is very significant. One more

A notable feature is that the assessee never divulged to the Assessing Officer the details and particulars of the claims despite specific enquiry. These two factors combine to lend to the case a colour different from the case relied upon on behalf of the assessee."

(at pages 172-73)

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The Bench distinguished the other decisions referred to before it by pointing out that the facts were entirely different in those cases. Hence, the ruling of the Calcutta High Court in the case cited will not help the appellant as it turned on the peculiar facts of the case as stated in the C passage extracted.

5. Learned counsel submits that the said judgment has been followed by the Calcutta High Court in *Commissioner of Income-Tax* v. *Jiajee Rao Cotton Mills Ltd.,* (1997) 227 ITR 860. There is no separate reasoning in D the said judgment and does not take the matter any further.

6. Learned counsel also referred to the judgment of the Bombay High Court in *Commissioner of Income-Tax* v. *Bennett Coleman and Co. Ltd.,* (1993) 201 ITR 1021. The Bench held that it was difficult to accept the contention of the assessee that cessation of liability can take place only E as a result of a bilateral act, but it will depend upon the facts of each case. The Bench pointed out that there may be cases where the liability is not barred by operation of law, but in such cases bilateral act of the parties will be necessary to bring about cessation of liability. According to the Bench, if the recovery had become barred by limitation by operation of F law, unilateral expression of intention of the debtor not to treat the amount any more as liability might be sufficient to bring about a cessation of the liability. The Bench also accepted the alternative argument that where an assessee had written off his time barred liability from his accounts and transferred the amount to his profit and loss account thereby treating it as his income, he could not be permitted to turn round when the question of G inclusion of such amount in his income under Section 41(1) of the Act arose. The Bench distinguished the judgment in *Kohinoor Mills Co. Ltd.* v. *CIT,* (1963) 49 ITR 578, by observing that there was no cessation of liability in that case despite the expiry of period of limitation to enforce the same. The Bench said that the assessee could not get rid of his liability when H called upon to meet either by the employees under the Industrial Disputes

Act or by the Government under the Bombay Welfare Fund Act on account of the special provisions of those Acts. We are unable to accept the reasoning of the Bombay High Court in that case. Just because an assessee makes an entry in his books of accounts unilaterally, he cannot get rid of his liability. The question whether the liability is actually barred by limitation is not a matter which can be decided by considering the assessee's case alone but it is a matter which has to be decided only if the creditor is before the concerned authority. In the absence of the creditor, it is not possible for the authority to come to a conclusion that the debt is barred and has become unenforceable. There may be circumstances which may enable the creditor to come with a proceeding for enforcement of the debt even after expiry of the normal period of limitation as provided in the Limitation Act.

7. One aspect of the matter has been completely ignored by the judgment of the Division Bench of the Bombay High Court. As pointed out already, the crucial words in the Section require that the assessee has to obtain in cash or in any other manner some benefit. That part of the Section has been omitted to be considered by the Division Bench of the Bombay High Court. The said words have been considered by a Full Bench of Gujarat High Court in detail in *The Commissioner of Income-tax, Gujarat-II, Ahmedabad* v. *M/s. Bharat Iron & Steel Industries, Bhavnagar,* (1993) Tax L R 188. The following passages in the judgment brings out of the reasoning of the Full Bench succinctly :

> "11. In our opinion, for considering the taxability of amount coming within the mischief of S. 41(1) of the Act, the system of accounting followed by the assessee is of no relevance or consequence. We have to go by the language used in s. 41(1) to find out whether or not the amount was obtained by the assessee or whether or not some benefit in respect of trading liability by way of remission or cessation thereof was obtained by the assessee and it is in the previous year in which the amount or benefit, as the case may be, has been obtained that the amount or the value of the benefit would become chargeable to income tax as income of that previous year.
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> 12. We fully agree with the view taken by the Division Bench in *C.I.T.* v. *Rashmi Trading,* (1977) Tax LR 520 Gujarat (Supra) that the only meaning that can be attached to the words "obtained, whether in cash or in any other manner whatsoever, any amount

A in respect of such loss or expenditure" incurred in any previous year clearly refer to the actual receiving of the cash of that amount. The amount may be actually received or it may be adjusted by way of an adjustment entry or a credit note or in any other form when the cash or the equivalent of the cash can be said to have been
B received by the assessee. But it must be the obtaining of the actual amount which is contemplated by the Legislature when it used the words "has obtained; whether in cash or in any other manner whatsoever, any amount in respect of such loss or expenditure in the past". As rightly observed by the Division Bench in the context in which these words occur, no other meaning is possible."

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we are in agreement with the said reasoning.

8. There is another judgment of the Bombay High Court which was rendered much earlier in *J.K. Chemicals Ltd.* v. *Commissioner of Income-Tax, Bombay City II,* (1966) 62 ITR 34. The Bench observed :
D

"..... The transfer of an entry is a unilateral act of the assessee, who is a debtor to its employees. We fail to see how a debtor, by his own unilateral act, can bring about the cessation or remission of his liability. Remission has to be granted by the creditor. It is
E not in dispute, and it indeed cannot be disputed, that it is not a case or remission of liability. Similarly, a unilateral act on the part of the debtor cannot bring about a cessation of his liability. The cessation of the liability may occur either by reason of the operation of law, i.e., on the liability becoming unenforceable at law by
F the creditor and the debtor declaring unequivocally his intention not to honour his liability when payment is demanded by the creditor, or a contract between the parties or by discharge of the debt - the debtor making payment thereof to his creditor. Transfer of an entry is neither an agreement between the parties nor payment of the liability. ....."

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(at page 41)

9. This judgment has been quoted by the High Court in the present case and followed. We have no hesitation to say that the reasoning is
H correct and we agree with the same.

10. The principle that expiry of period of limitation prescribed under the Limitation Act could not extinguish the debt but it would only prevent the creditor from enforcing the debt, has been well settled. It is enough to refer to the decision of Court in *Bombay Dyeing & Manufacturing Co. Ltd.* v. *The State of Bombay and Others,* [1958] SCR 1122. If that principle is applied, it is clear that mere entry in the books of accounts of the debtor made unilaterally without any act on the part of the creditor will not enable the debtor to say that the liability has come to an end. Apart from that, that will not by itself confer any benefit on the debtor as contemplated by the Section.

11. In the circumstances, we find no merit in this appeal and it is dismissed. There will be no order as to costs.

T.N.A. Appeal dismissed.