

IN THE HIGH COURT OF KERALA AT ERNAKULAM

PRESENT :

THE HONOURABLE MR. JUSTICE C.N.RAMACHANDRAN NAIR
&

THE HONOURABLE MR. JUSTICE T.R.RAMACHANDRAN NAIR

MONDAY, THE 4TH FEBRUARY 2008 / 15TH MAGHA 1929

ITA.No. 181 of 2001()

ITA.492/COCH/1996 of I.T.A.TRIBUNAL,COCHIN BENCH
.....

APPELLANT:

THE COMMISSIONER OF INCOME TAX,
TRICHUR.

BY ADV. SRI.P.K.R.MENON(SR.),SC FOR IT
SRI.GEORGE K. GEORGE, SC FOR IT

RESPONDENTS:

M/S.KERALA SOLVENT EXTRACTIONS LTD.,
IRINJALAKUDA, TRICHUR.

BY ADV. SRI.P.BALACHANDRAN
SMT.PREETHA S.NAIR

THIS INCOME TAX APPEAL HAVING BEEN FINALLY HEARD
ON 04/02/2008, THE COURT ON 04/02/2008 DELIVERED THE
FOLLOWING:

C.R.

C.N.RAMACHANDRAN NAIR &
T.R.RAMACHANDRAN NAIR, JJ.

.....
I.T.A. No.181 of 2001

.....
Dated this the 4th day of February, 2008.

JUDGMENT

C.N.Ramachandran Nair, J.

This is an appeal filed by the Revenue under Section 260A of the Income Tax Act challenging the order of the Income Tax Appellate Tribunal confirming cancellation of proceedings under Section 143(1)(a) by the C.I.T.(Appeals) pertaining to disallowance of sales tax payments made by the assessee. In the accounting year relevant for the assessment year 1994-95, the assessee which was following the mercantile system of accounting, made additional payment of Rs.23 lakhs towards sales tax payable for April 1994. Since it was specifically stated in the statement of accounts accompanying the return that the amount paid was towards sales tax payable for April 1994, the Assessing Officer disallowed the claim and computed tax liability. The assessee objected against disallowance under Section 143(1)(a) of the Act by filing a rectification application under Section 154 of the Act which was rejected by the Assessing Officer. In the appeal filed against this order, the CIT (Appeals) allowed the claim holding that

disallowance of amount paid towards advance sales tax is a debatable point. This was confirmed by the Tribunal against which this appeal is filed by the Revenue. We have heard Standing Counsel for the Income Tax Department appearing for the appellant and Sri.P.Balachandran, Senior counsel appearing for the respondent-assessee.

2. While Standing Counsel contended that the amount paid being sales tax liability payable in April 1994 is not an allowable deduction under Section 37(1) read with Section 145 of the Income Tax Act, Senior counsel for the respondent-assessee contended that the tax having been paid in the previous year, though not liability of the year, is an allowable deduction under Section 43B(a) read with Explanation 2 to the said Section. Standing Counsel referred to decision of this court in COMMISSIONER OF INCOME TAX V. SITARAM TEXTILES LTD. (2001) 248 ITR 139 and contended that the claim is not allowable as assessee has not incurred expenditure. The specific case of the department is that unless the amount paid is liability of the assessee for the previous year, it cannot be allowed, no matter the assessee has paid it or not. In order to appreciate the contentions, we have to refer to Section 43B, the relevant clauses of which are extracted hereunder:

"S.43B.Certain deductions to be only on actual payments:

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

(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) 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, or

(c) any sum referred to in clause (ii) of sub-section(1) of section 36, or

(d) any sum payable by the assessee as interest on any loan or borrowing from any public financial institution or a State financial corporation or a State industrial investment corporation, in accordance with the terms and conditions of the agreement governing such loan or borrowing, or

(e) any sum payable by the assessee as interest on any term loan from a scheduled bank in accordance with the terms and conditions of the agreement governing such loan, or

(f) any sum payable by the assessee as an employer in lieu of any leave at the credit of his employee,

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:

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) or clause (e) or clause (f) 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 such return:

Provided further that no deduction shall, in respect of any sum referred to in clause (b), be allowed unless such sum has actually been paid in cash or by issue of a cheque or draft or by any other mode on or before the due date as defined in the Explanation below clause (va) of sub-section (1) of section 36, and where such payment has been made otherwise than in cash, the sum has been realised within fifteen days from the due date".

It is not in dispute that sales tax liability of the assessee is an allowable deduction in the computation of income from business by virtue of Section 29 read with Section 37(1) of the Income Tax Act. Among other things it is stated in Section 145 of the Income Tax Act that income chargeable under the head "profits and gains of business or profession" should be computed in accordance with either cash or mercantile system of accounting regularly employed by the assessee. The assessee is admittedly following the mercantile system of accounting and therefore, sales tax liability like any other liability should be claimed and allowed on mercantile basis. In other words, liability of the relevant previous year only should be allowed as a deduction. Assessee itself admitted in the return and the statement of accounts filed that the amount of Rs.23 lakhs paid is the sales tax liability of April 1994 which obviously means that the liability is that of the next financial year. Going by Section 145, the assessee was not entitled to deduction of this amount paid to the Sales Tax Department. However, the

question is whether Section 43B entitles the assessee for deduction of liability of the next financial year merely because the amount is paid by the assessee during the previous year relevant for the assessment year. We are unable to uphold assessee's contention because Section 43B in itself is not a provision providing for deduction of any item of expenditure which is otherwise not allowable under any of the provisions of the Act. The opening words of Section 43B extracted above clearly shows that the Section is dealing with deductions otherwise allowable under provisions of the Act. The Section only lays down conditions for eligibility for deduction of certain allowances which are otherwise admissible under the Act. The scheme of Section 43B is to allow the deductions referred to in clauses (a) to (f) only on payment basis, even though assessee is following mercantile system of accounting. In other words, it is an exception to Section 145 of the Act in as much as even if the claim is an allowable deduction of the assessee, based on system of accounting followed by the assessee, it will still be inadmissible under Section 43B if it is not paid on or before the end of the relevant previous year or atleast before date of filing of the return. Therefore, Section 43B is only supplementary to Section 145 and it is only an additional condition for allowance of deductions otherwise allowable under the other provisions of the Act. The scheme of payment of

sales tax under the Sales Tax Act of the State is to remit tax due for every month on or before the 10th of the succeeding month. The only exception to this is the payment of advance tax for the last month of the financial year on or before 30th of March. Therefore, the liability towards sales tax for an assessee is the tax payable along with monthly returns and final return and the tax otherwise assessed, demanded and payable by the assessee in the previous year. If the assessee remits any amount in the financial year towards tax payable for any month of the next financial year, the said amount does not constitute tax liability of the assessee for that previous year. On the other hand, it will be carried as an amount of tax paid in advance for the next year and if assessee carries on business and incurs liability in the next year, the amount will be adjusted towards tax liability for that year. On the other hand if the assessee does not continue business, it is entitled to get refund of the tax paid in the previous year. The assessee itself has conceded in the statement of accounts that Rs.23 lakhs paid was to be adjusted towards sales tax liability for April 1994 which is the first month of the next financial year. Explanation 2 to Section 43B relied on by the assessee will not justify the assessee to claim deduction because under the said provision only liability incurred by the assessee during previous year is allowable on payment basis. Here again, what the

explanation contemplates is incurring of liability by the assessee in the previous year, though the amount is not payable during the previous year under the relevant law. So far as sales tax is concerned, it is a tax on sale or purchase of commodity. Since the liability falls under the statute and since the assessee has no case that the remittance was towards tax due for the previous year or payable in that year, the assessee is not entitled to claim deduction under Section 29 read with Section 37(1) and Section 145 of the Income Tax Act. As already held, Section 43B in itself does not help the assessee to claim deduction as it is only an additional condition for allowing deduction which is otherwise admissible under the provisions of the Act.

3. The next question to be considered is whether the Assessing Officer was justified in disallowing the claim and computing tax liability under Section 143(1)(a) of the Act. Even though the C.I.T.(Appeals) and the Tribunal held that the question whether the amount payable by the assessee in the previous year being sales tax liability is a debatable issue which cannot be decided in proceedings under Section 143(1)(a), we are unable to uphold the orders of the two authorities because clause (iii) of first proviso to Section 143(1)(a)(ii) authorises the Assessing Officer to compute tax or interest payable by or in favour of the assessee among other things after making adjustments in the income or loss declared in the return

which includes addition of any deduction claimed which is "prima facie inadmissible". The question whether an item is prima facie inadmissible or not has to be found out from the return and statement of accounts furnished by the assessee. If deduction claimed is not allowable even according to the statement of the assessee, then it is a prima facie inadmissible deduction which can be added back in proceedings under Section 143(1)(a) of the Act. In this case assessee itself made statement that the amount claimed is sales tax liability of April of the next financial year. In other words, assessee had conceded that the liability is that of the next year and so much so, on the basis of assessee's statement itself it was clear that the amount is prima facie inadmissible as a deduction towards tax liability. Therefore, we find that the Assessing Officer needed no clarification for making disallowance because assessee itself conceded that it is a liability of the next financial year. We are therefore of the view that the item disallowed is one prima facie inadmissible and hence the Assessing Officer was perfectly justified in disallowing the claim in the proceedings completed under Section 143(1)(a) of the Act. In fact, under the scheme of Sales Tax Act in the computation of liability for the previous year, the amount paid will be just refunded to the assessee as excess tax paid for adjustment towards liability for next year. Therefore, even if the assessee's

claim was allowed by mistake by the Officer, the amount is assessable in the next year based on refund as provided under Section 41(1) of the Income Tax Act. Therefore, we are of the view that the Tribunal clearly committed an error in confirming the first appellate authority's order allowing petitioner's claim. The appeal is therefore allowed vacating the order of the Tribunal and confirming the order of the officer rejecting application to rectify proceedings under Section 143(1)(a) of the Act.

C.N.RAMACHANDRAN NAIR
Judge

T.R.RAMACHANDRAN NAIR
Judge

pms