

2017 (5) TMI 1221 - CALCUTTA HIGH COURT**M/s. Shivlaxmi Exports Ltd. Versus Commissioner of Income Tax, W.B.**

ITA No. 134 of 2001

Dated: - 30 March 2017

Addition on waiver of interest - accrual of income - debtors' inability to pay the interest for years - Tribunal in the rectification proceeding rejected assessee plea on the ground that it maintained mercantile system of accounting, the debts were not declared as bad debts and the assessee continued to receive back the principal sums from the borrowers - Held that:- Mere following of mercantile system ought not to result in accrual of income from interest when there is no interest income in real terms and the statements of account of the assessee also did not reflect any credit entry in respect of interest receipt from the aforesaid borrowers. Commercial decision was taken by the appellant-assessee not to charge interest from these two borrowers as the assessee wanted to ensure recovery of the principal sums lent. In absence of realization of real income and there being no accrual of such income subsequent to the aforesaid Board resolutions, interest income could not be added to the income of the assessee for the relevant financial year

We find the points of law involved in this appeal are covered by Shoorji Vallabhdas (1962 (3) TMI 6 - SUPREME Court) and Poona Electric (1965 (4) TMI 20 - SUPREME Court). The interest income could not said to have had accrued for the appellant for the assessment year in the background of the resolutions taken for waiver of interest. - Decided in favour of the assessee.

Judgment / Order**Aniruddha Bose And Arindam Sinha, JJ.****Mr.G.R.Sharma,Advocate For the Appellant****Mr.Prabir Bhowmick, Mr.P. Dudheria, Mr. Yogesh Vats, Advocates For the Respondent****ORDER**

The Court : After hearing the appellant-assessee, we admit the appeal on the following two questions as suggested by the assessee.

"1. Whether on the facts and in the circumstances of the case Tribunal was right in confirming the addition of interest, though waived by the assessee on account of the debtors' inability to pay the interest for years simply on the score that the assessee follows the mercantile method of accounting.

2. Whether the Tribunal's order is replete with incongruities and vitiated for being founded on a wrong premise that there was no resolution passed by the Board of Directors for the waiver and such premise being based on no evidence and inconsistent with the orders of the lower authorities as also the circumstances of the case, renders the order perverse."

We are satisfied that these two points involve substantial questions of law, and hence we admit the appeal on these two points:

2. The assessee is an incorporated company and at the material point of time, its income, inter alia, was from interest and commission. The present appeal is in relation to waiver of interest of two of its borrowers, Shroff Chemicals Pvt. Ltd. and Eastern Commercial Enterprises. Loans were advanced to these two borrowers during the financial year 1985-86. Admitted position is that the assessee maintains its accounts on mercantile basis. It is the assessee's case that these two borrowers had made request for not charging any interest at the material point of time and this request was acceded to by the assessee.

3. In a supplementary affidavit filed before us affirmed by one Ajoy Kr. Agarwal on 22nd June, 2001, the board resolutions of the company taken on 15th May, 1987 have been annexed. These resolutions relate to waiver of interest of these two borrowers and provide:-

“RESOLVED that the petition received from M/s. Shroff Chemicals Pvt. Ltd. vide letter dated 04/04/87 for waiver of interest on loan due to acute financial stringency/crisis be and is hereby accepted and it was decided not to charge any interest on the outstanding amount of ₹ 2,03,708.97 from this financial year and onward.

RESOLVED that the petition received from M/s. Eastern Commercial Enterprises vide letter dated 13/04/87 for waiver of interest on loan due to acute financial stringency/crisis be and is hereby accepted and it was decided not to charge any interest on the outstanding amount of ₹ 2,64,238.00 from this financial year and onward.”

4. The assessee did not credit any interest in respect of these two borrowers in its books thereafter uptill and including the assessment year 1990-91, in respect of which assessment year the controversy has given rise to this appeal. For the assessment years previous to the assessment year under consideration, no question was raised as regards the waiver of interest in relation to these two borrowers. In the subject assessment year, the assessing officer directed addition to the income of the assessee ₹ 1,08,883/- as interest income from Shroff Chemicals Pvt. Ltd. and ₹ 39,635/- from Eastern Commercial Enterprises.

Appeal against assessment for that year was preferred by the assessee on various grounds. So far as the present proceeding is concerned, the subject of dispute relates to the addition of income in respect of the aforesaid two borrowers. The plea of the assessee was rejected by the CIT(A), inter alia, on the following ground.

“In the last ground the appellant objected to the addition of notional interest from the two parties as unfair and improper since the same could not be realised from 1987.

It is observed that the assessee is following mercantile system of account and therefore, interest amount on the basis of prevailing market rate has rightly been added on due basis. The addition on this score is, therefore, confirmed.”

5. The assessee appealed before the Tribunal assailing the Commissioner's decision. The Tribunal, in a judgment delivered on 4th December 2000 rejected the appellant's stand on this point and held:-

“We heard both parties and gone through the materials available on record, from which it appears that the assessee has advanced the loan to M/s. Shroff Chemicals (P) Ltd. on interest. The assessee was following the mercantile system of accounting. During the assessment years 1985-1986 and 1986-1987, the interest was credited in the books of accounts. But after receiving a request, the assessee stopped this practice and did not credit the interest for the remaining period. But the fact

remains that the assessee continues to receive back the principal amount from the said Company. For waiving the interest, no resolution was passed by the Board of Directors. It also reveals from the record that the said debt was not a bad-debt as time to time payment was received by the assessee-company. It is the business of the assessee to have the income from interest.”

Learned Counsel for the assessee apprises us that the assessee had brought a rectification proceeding under Section 254 of the 1961, Act seeking in substance deletion of the interest income from the assessment order in relation to the aforesaid borrowers. It is his contention that in that proceeding, the assessee sought to bring on record that the Board had passed resolutions to that effect. The rectification application was registered as MA No.47 (Cal) of 2001 and was rejected by an order dated 8th June, 2001 in the following terms:

“4. After hearing both the parties and on perusal of the record, we are of the view that the main grievance of the assessee is regarding the observations made by the Tribunal that –

‘No resolution was passed by the Board of Directors for waiving the interest.’

In fact, this observation was submitted by the learned Departmental Representative during the course of argument as the same is reflected in para 6 (at pages 2-3 of the Tribunal’s order). Thus, the Tribunal suo motu has not imported this observation. Even without this observation, the Tribunal was justified in dismissing the assessee’s appeal on merit.

5. Needless to mention that the law takes no account of every trifling matters as per the maxim – ‘Ded Minimis Non Curat Lex’

6. In the light of above discussion, we are of the view that there is no mistake apparent from the record. Hence, the Miscellaneous Application filed by the assessee has no merit.

7. In the result, the Miscellaneous Application filed by the assessee is rejected.”

6. From the order of the Tribunal assailed before us, and the order passed by the Tribunal in the rectification proceeding, it becomes apparent that the plea of the assessee was primarily rejected on the ground that it maintained mercantile system of accounting, the debts were not declared as bad debts and the assessee continued to receive back the principal sums from the borrowers.

On behalf of the assessee, it is submitted before us that waiver of interest was accepted by the respective Assessing Officers in the earlier assessment years subsequent to the passing of the resolution by the Board. It is further submission of Mr. Sharma, learned advocate for the assessee that the decision to waive interest was taken on the basis of commercial expediency, having regard to the reasons reflected in the resolutions themselves and these resolutions were duly taken. He has argued that mere following of mercantile system ought not to result in accrual of income from interest when there is no interest income in real terms and the statements of account of the assessee also did not reflect any credit entry in respect of interest receipt from the aforesaid borrowers. It is his specific case that commercial decision was taken by the appellant-assessee not to charge interest from these two borrowers as the assessee wanted to ensure recovery of the principal sums lent. In absence of realization of real income and there being no accrual of such income subsequent to the aforesaid Board resolutions, interest income could not be added to the income of the assessee for the relevant financial year. He has relied on the cases of Commissioner of Income Tax vs. Birla Gwalior Pvt. Ltd., reported in [1973] 089 ITR 0266 (SC). The Hon’ble Supreme Court in this decision has relied on two previous authorities being C.I.T. vs. Shoorji Vallabhdas & Co., [1962] 46 ITR 144 and Poona Electric Supply Co. Ltd. vs. CIT [1965] 57 ITR 521.

7. In the case of Shoorji Vallabhdas (Supra), the Supreme Court held:-

“Income-tax is a levy on income. Though the Income-tax Act takes into account two points of time at which the liability to tax is attracted, viz., the accrual of the income or its receipt, yet the substance of the matter is the income. If income does not result at all, there cannot be a tax, even though in book-keeping, an entry is made about a ‘hypothetical income’, which does not materialise. Where income has, in fact, been received and is subsequently given up in such circumstances that it remains the income of the recipient, even though given up, the tax may be payable. Where, however, the income can be said not to have resulted at all, there is obviously neither accrual nor receipt of income, even though an entry to that effect might, in certain circumstances, have been made in the books of account.”

In Poona Electric (Supra), the same principle of law was reiterated.

The other authority which is relied on by Mr. Sharma is a Bench decision of this Court in the case of Sri Kewal Chandra Bagri vs. Commissioner of Income Tax, [1990] 53 Taxman 536 [Cal].

8. Though the three decisions of the Supreme Court to which we have referred to arose out of construction of the Income Tax Act, 1922, so far as the point in issue is concerned, the same principle applies under the 1961 Act also. The Bench decision of this Court in the case of Sri Kewal Chandra Bagri (supra), was delivered construing the provisions of 1961 Act, relying on the judgements of the Hon’ble Supreme Court in the case of Poona Electric Supply Co. Ltd. (supra) and Shoorji Vallabhdas (supra).

9. Mr. Bhowmick, learned advocate appearing on behalf of the Revenue has contested this appeal. His submission is that since the borrowers’ dues were not declared bad debts and the assessee had applied the mercantile system of accounting, the assessing officer had rightly added the interest income as having accrued for the relevant assessment year. He has relied upon the case of Commissioner of Income Tax vs. Shiv Prakash Janak Raj and Co. Pvt. Ltd., [(1996) 222 ITR 583]. He has invited our attention to the following passage from that said judgment:-

“The concept of real income cannot be employed so as to defeat the provisions of the Act and the Rules. Where the provisions of the Act and the Rules apply, it is only those provisions which must be applied and followed. There is no room – nor would it be permissible for the court – to import the concept of real income so as to whittle down, qualify or defeat the provisions of the Act and the Rules.”

In the case of Shiv Prakash (Supra) the following two questions were examined for consideration; which appears from that judgment itself:-

“(i) Whether, on the facts and in the circumstances of the case, the Tribunal was right in holding that the interest for the assessment year 1971-72, had already accrued to the assessee on October 31, 1970, under the mercantile system of accountancy?

(ii) Whether, on the facts and in the circumstances of the case, the Tribunal was right in holding that the subsequent relinquishment of interest by a resolution dated November 24, 1970, did not affect the tax liability of the assessee on accrual basis?”

10. As would be evident from the questions framed in that appeal, the resolutions relinquishing interest were taken subsequent to accrual of interest in the financial years in question. The Hon’ble Supreme Court recorded the following facts as being involved in that decision, distinguishing the applicability of the ratios of

the judgments in the case of Birla Gwalior (supra) and Poona Electric (supra) and Shoorji Vallabhdas (supra):-

“Before we refer to the decisions of this Court, it is necessary to reiterate the basic facts of the case. For the previous two assessment years, viz., 1966-67 and 1967-68, the assessee-company did charge interest on the loan advanced by it to the firm which shows that the loan was an interest bearing loan. The second circumstance to be noticed is that the resolution waiving interest was passed after the expiry of the relevant accounting year in the case of the three subsequent assessment years, viz., the assessment years 1969-70, 1970-71 and 1971-72. Only in the case of the assessment year 1968- 69, was the resolution passed before the expiry of the accounting year. Thirdly, the assessee-company was maintaining its accounts on the mercantile basis. Yet, another circumstance to be noticed is that the Tribunal has found it as a fact that the waiver was not based upon any commercial considerations. Of course, no entries were made in the accounts of the assessee-company, or for that matter in the accounts of the firm, in respect of the four assessment years concerned herein, that any interest was received or paid. On these facts, it has to be held that in the case of the three subsequent assessment years, the interest had accrued to the assessee notwithstanding the fact that no entries may have been made in the accounts of the assessee to that effect. The waiver of interest after the expiry of the relevant accounting year only meant that the assessee was giving up the money which had accrued to it. It cannot be said, in the circumstances, that the interest amount had not accrued to the assessee. Therefore, the Tribunal was right in taking the view it did in respect of the assessment years 1969-70, 1970-71 and 1971-72. In the case of the assessment year 1968-69, however, the resolution was passed before the expiry of the accounting year and though the finding of the Tribunal is that the said waiver was not actuated by any commercial considerations, yet learned counsel for the Revenue did not press the Revenue’s case so far as this assessment year is concerned.”

11. One basic distinguishing feature so far as the factual background of the present appeal is concerned vis-à-vis the case of the assessee in the decision of the Hon'ble Supreme Court in the case of Shiv Prakash (supra) is that the assessee in this appeal had taken resolution prior to the assessment year under consideration. There is no dispute that it was a decision of the assessee based on commercial consideration. Unlike the case of Shiv Prakash (supra) in which it was found that partners of the borrowing firm and the shareholders/directors of the assessee company were same, the records of this appeal do not show any linkage or nexus between the assessee and its two borrowers.

12. In this perspective, we find the points of law involved in this appeal are covered by Shoorji Vallabhdas (supra) and Poona Electric (supra). The interest income could not said to have had accrued for the appellant for the assessment year in the background of the resolutions taken for waiver of interest.

We, accordingly, answer the questions in favour of the assessee. The appeal and the application are allowed in the above terms, and the decision of the Tribunal is set aside.

There shall be no order as to costs.

Citations: in 2017 (5) TMI 1221 - CALCUTTA HIGH COURT

1. [Commissioner of Income-Tax Versus Shiv Prakash Janak Raj And Company Private Limited - 1996 \(9\) TMI 5 - SUPREME Court](#)
2. [Commissioner of Income-Tax, West Bengal II Versus Birla Gwalior Private Limited - 1973 \(4\) TMI 2 - SUPREME Court](#)
3. [Poona Electric Supply Company Limited Versus Commissioner Of Income-Tax, Bombay City I - 1965 \(4\) TMI 20 - SUPREME Court](#)
4. [Commissioner Of Income-Tax, Bombay City I Versus Messrs. Shoorji Vallabhdas And Company - 1962 \(3\) TMI 6 - SUPREME Court](#)
5. [Sri Kewal Chand Bagri Versus Commissioner Of Income-Tax - 1989 \(6\) TMI 23 - CALCUTTA High Court](#)