

# ANDHRA PRADESH HIGH COURT

Khan Bahadur Ahmed Alladin & Sons

Vs

Commissioner of Income-Tax

(P Jaganmohan Reddy,CJ. R Rao, J.)

25.11.1968

## JUDGMENT

**Jaganmohan Reddy, C.J.**

1. The Income-tax Appellate Tribunal has referred the following two questions for our opinion, namely :

"1. Whether the purchase of the site and the buildings known as "Bregun Estate" was in the course of a profit-making scheme or adventure in the nature of trade ?

2. If the answer to question No. 1 is in the affirmative, whether the extra compensation of Rs. 99,245 awarded by the District Judge on 12th July, 1956, is assessable for the assessment year 1955-56 ?"

2. The assessee, a firm registered under Section 26A of the Income-tax Act, 1922, was being assessed to income-tax for the year 1955-56, for which the corresponding accounting year was from 1st October, 1953, to 30th September, 1954, in which accounting year the second of the questions arose. It appears that the assessee-firm bought from the Government of India a property known as "Bregun Estate" consisting of factory and other buildings along with 403 acres of open land, some of which were sold in the previous years and the profits arising from such sales were held to be liable to income-tax as arising from business. In respect of a further portion of this land, viz., 36 acres and 6 guntas, the Government of Hyderabad, after duly notifying the same, acquired it under Section 3(1) of the Hyderabad Land Acquisition Act, and subsequently took over possession of the same on 23rd June, 1954, after making the necessary declaration under Section 6, The Collector by his award under Section 10 of the Act dated 10th December, 1954, fixed the compensation payable to the-assessee at O.S. Rs. 1,25,131 at the rate of Rs. 3,000 per acre. This amount was paid to the assessee on 22nd March, 1956. Aggrieved by the award, the assessee requested the Collector to make a reference to the District Judge, and on

the same being made, the District Judge enhanced the value from Rs. 3,000 to Rs. 5,000 per acre, which enhanced the compensation payable to the assessee by Rs. 99,245. Against this order, it is stated, though the statement of the case does not mention it, for the sake of completion of the narration of facts, we give this further fact, though not relevant for our purpose, viz., that there was an appeal to the High Court, which was dismissed. It may be remembered that the compensation of Rs. 1,25,131 was paid on 22nd March, 1956, and was, therefore, accountable in the year relevant for 1957-58 assessment. The Income-tax Officer accordingly made assessment including the compensation in that year. True assessee: filed an appeal against that order, on the ground that the compensation was not includible in that assessment, as the sale had actually taken place in July, 1954, and the Collector had taken possession of the land. The Appellate Assistant Commissioner accepted the assessee's contention and directed the Income-tax Officer to assess the taxable profit for the assessment year 1955-56. Accordingly, the Income-tax Officer reopened the assessment for 1955-56 under Section 34 of the Income-tax Act, 1922. In this assessment, he included a net profit of Rs. 1,75,533 (I.G.) worked out on the basis of the total compensation amounting to O.S. Rs. 2,24,016 (which includes the enhanced compensation of Rs. 99,245) awarded by the District Judge. The assessee appealed against this order. Before the Appellate Assistant Commissioner it was contended (i) that no part of the profit was taxable as it did not arise from the carrying on of a business and (ii) that the additional compensation awarded by the District Judge should not be included as it had not accrued in that accounting year. It may be mentioned that the compensation originally fixed by the Collector was a receipt in the accounting year and was, if at all, assessable in that year. The Appellate Assistant Commissioner decided the first point against the assessee, following the order of the Tribunal for the earlier years, and on the second point, he agreed with the assessee's contention and held that the additional compensation accrued to the assessee only on 12th July, 1956, which was the date of the order of the District Judge. The additional compensation of Rs. 99,245 was therefore ordered to be deleted. The Appellate Tribunal however, on appeal by both the assessee and the department--the assessee in respect of the finding on the first question and the department as against the finding on the second question--held that the surplus realised by the assessee was a business profit, following its earlier order, which was the subject-matter of a reference in this court in R. C. No. 42 of 1962. On the second question, the Tribunal held that the lands formed the stock-in-trade of the assessee's business and, as such the realisation either from sale or acquisition by the Government would represent only a business receipt. It further held that the enhanced compensation accrued to the assessee on 23rd June, 1954, when the land was taken possession of by the Collector. Consequently, it allowed the appeal of the department.

3. On the first question referred, we may observe that this court had already in R.C. No. 42/62 decided on 23rd July, 1964 (to which one of us, the Chief Justice, was a party), answered the question against the assessee holding that the purchase of the site was an adventure in the nature

of trade and was in the course of a profit-making scheme. Against this decision, the assessee went up in appeal to the Supreme Court which in Khan Bahadur Ahmed Alladin and Sons v. Commissioner of Income-tax, affirmed the decision of this court. Accordingly, the first question will have to be answered in the affirmative and in favour of the department.

4. On the second question, Sri Anjaneyulu, on behalf of the assessee, contends that the relevant year of assessment for the enhanced compensation was the year in which the compensation was awarded and not the year in which the possession of the land was taken. He has cited several decisions, to which we shall presently refer. Secondly, he contends that once compensation has been included in an year of assessment there is no power in the Income-tax Officer to reopen it and therefore there is no way in which he could include the enhanced compensation ordered to be paid subsequently by the court.

5. Sir Ananta Babu, for the department, contends that the right to compensation accrues on the date when possession is taken, and, therefore, whether it is the compensation awarded by the Collector or the subsequently enhanced compensation, they must all be included in the year in which the compensation was awarded by the Collector, as that is the year in which the assessee was entitled to receive the same.

6. On a consideration of the nature of acquisition proceedings, it appears to us that when lands are notified to be taken by the Government under the Land Acquisition Act, the owner of the land is entitled to payment of compensation at the market value on the date when possession was taken pursuant to a notification under Section 3 of the Hyderabad Land Acquisition Act. It may be stated that on the date when land is taken possession of by the Government, no compensation has in fact been determined, but it has become only payable. The right of the owner is, therefore, an inchoate right. It is like, to borrow a term applicable to movable properties, a chose-in-action, i.e., a present right to take proceedings to recover a debt or damages, and thus inchoate in the sense that the compensation has not in fact been determined or become payable. In so far as the Income-tax Act is concerned, an income is assessable to charge only when it accrues or arises or is deemed to accrue or arise in the year of assessment. Section 4(1)(b)(i) of the Income-tax Act, 1922, which uses the words "accrue or arise" is as follows :

"Subject to the provisions of this Act, the total income of any previous year of any person includes all income, profits and gains from whatever source derived which--.....

(b) if such person is resident in the taxable territories during such year,--

(1) accrue or arise or are deemed to accrue or arise to him in the taxable territories during such year ... ."

7. We may, even at the risk of repetition, state that the compensation, which has been treated in this case as profits from an adventure in the nature of trade, is payable to the assessee. But the question is : Has it accrued or is deemed to accrue to him ? It may, in some circumstances, where an amount becomes payable, be deemed to have accrued to him even though in fact it is not paid but paid subsequently. But unless the income is determined and becomes payable, merely to have a right to receive compensation or payment of an unspecified amount does not attract tax liability in the year in which the assessee gets such a right. Bhagawati J., delivering the judgment of their Lordships of the Supreme Court in E. D. Sassoon & Co. Ltd. v. Commissioner of Income-tax, , accepted the definition given to the words "accrue" or "arise" by Mukerji J. in *Rogers Pyatt Shellac & Co. v. Secretary of State for India*<sup>1</sup>, which definition has again been referred to and approved of by Subba Rao J. (as he then was) in *Commissioner of income-tax v. A. Gajapathy Naidu*, .

8. In *Rogers Pyatt Shellac & Co. v. Secretary of State for India* Mukerji J. dealt with the terms "accrues", "arises" and "is received" and, after citing a judgment of Fry L.J. in *Colquhoun v. Brooks*<sup>2</sup>, said : "....., both the words" (i.e., "accrues" and "arises") are used in contra-distinction to the word "receive" and indicate a right to receive. They represent a stage anterior to the point of time when the income becomes receivable and connote a character of the income which is more or less inchoate". In *Gajapathi Naidu's* case Subba Rao J., after stating that if an income accrues within a particular year, it is liable to be assessed in the succeeding year, asked the question : When does the right to receive an amount under a contract accrue or arise to the assessee, i.e., come into existence? After noticing that under the English law it is said that on the basis of proper commercial accounting practice, if a transaction takes place in a particular year, all that has accrued in respect of it, irrespective of the year when it accrues, should belong to the year of transaction and, for the purpose of reaching that result, closed accounts could be reopened, his Lordship observed at page 119 :

"Whether this principle is justified in the English law, it has no place under the Indian Income-tax Act. When an Income-tax Officer proceeds to include a particular income in the assessment, he should ask himself, inter alia, two questions, namely : (i) what is the system of accountancy adopted by the assessee ? and (ii) if it is the mercantile system of accountancy, subject to the deemed provisions, when has the right to receive that amount accrued ? If he comes to the conclusion that such a right accrued or arose to the assessee in a particular accounting year, he shall include the said income in the assessment of the succeeding assessment year. No power is conferred on the Income-tax Officer under the Act to relate back an income that accrued or arose in a subsequent year to another earlier year on the ground that the said income arose out of an earlier transaction."

9. The deeming provision can have no relevance unless the income is receivable, and once it is receivable, then the determination of the question whether it is actually received or is deemed to have been received might depend upon the system or method of accounting. But before ever the right to receive a particular amount as income accrues, no charge can be levied on that amount in any year anterior to the one in which it is receivable.

10. A decision of this court in *Mahalakshmi Rice & Oil Mill v. Commissioner of Income-tax*<sup>3</sup>, was cited by the learned advocate for the assessee as supporting his contention. There the assessee-firm carried on the business of milling paddy into rice and selling it. On the 9th May, 1954, the assessee was appointed as the procuring agent by the Government for procuring paddy under the voluntary procurement of paddy and compulsory procurement of paddy schemes. After procuring the paddy, the assessee had to mill it into rice and hold the stocks on behalf of the Government. One of the conditions of the agreement was that the assessee shall not dispose of the stocks of paddy and/or rice held by the assessee on behalf of the Government, except under and in accordance with the directions of the District Collector or any officer authorised by him. The assessee was to be paid for the rice so exported at certain rates appended to the agreement. Later, however, the Government felt that they were not in need of further stocks of rice and an agreement was reached between the assessee and the Government to permit the assessee to dispose of the stocks at the assessee's own risk against payment of a suitable compensation which was fixed at Rs. 2-6-0 per maund. On the basis of this order, a sum of Rs. 44,000 was paid to the assessee in July, 1955. It was held that this amount was properly included in the income-tax return for 1956-57 assessment. This, of course, is a reverse case.

11. Sri Ananta Babu, however, tries to distinguish this case on the ground that in that case the payment was an ex gratia payment, and relies on a passage in the judgment of Chandra Reddy C.J., at page 470. After referring to certain observations of Lord Hanworth *M.R. in Bernhard v. Gahan* (*H.M. Inspector of Taxes*<sup>4</sup>), Chandra Reddy C.J. said at page 470 :

"It is manifest from this passage that it is only when a right has accrued or a liability created in a particular year, the income can be said to have accrued or liability created in the year in spite of the fact that the ascertainment of the amount or the receipt of it is postponed to a subsequent date. It cannot be posited that an ex gratia payment is the result of a right."

12. These observations cannot be divorced from the actual decision in that case. If it is contended that those observations have the effect of imposing a tax liability in respect of a right to receive payment, even though the amount has not been ascertained or a debt accrued, then the tax liability can be said to accrue on the date when possession of the land is taken by the Government under the Land Acquisition Act, on which date, as we have said earlier, the assessee

has merely an inchoate right to have the compensation determined. What is the income that can be said to have accrued to him on that date which can be assessed to tax in the year of assessment ? If the actual amount of compensation has not been fixed, no income could accrue to him. It cannot be contended that the mere claim by the assessee, after taking of possession, at a particular rate or for a certain sum is the compensation. It is the amount actually awarded by the Collector or subsequently decreed by the court which accrues to him, and the respective amounts, whether awarded by the Collector or the court accrue on the respective dates on which the award or the decree is passed. Income-tax is not levied on a mere right to receive compensation ; there must be something tangible, something in the nature of debt, something in the nature of an obligation to pay an ascertained amount. Till such time, no income can be said to have accrued. If we may say so with respect, the learned judges in Mahalakshmi Rice & Oil Mill case appear to have relied to a large extent on certain English cases, namely. *Commissioners of Inland Revenue v. Newcastle Breweries Ltd.*<sup>5</sup>, *Commissioners of Inland Revenue v. Gardner, Mountain and D' Ambrwmenil Ltd*<sup>6</sup>, etc., with respect to which this court has, on several occasions, observed--which observations are reinforced by their Lordships of the Supreme Court--that it is not advisable to rely upon English decisions in interpreting the Indian Income-tax Act. We have already noticed the observations of Subba Rao J. (as he then was) in Gajapathy Naidu's case. In the same judgment, after referring to *J. P. Hall and Co. v. Commissioners of Inland Revenue*<sup>7</sup>, and *Severne v. Dadswell*<sup>8</sup>, and stating that they would prefer to base their conclusions on the meaning of the words "accrue" and "arise" in Section 4(1)(b)(i) of the Income-tax Act, observed at page 121 :

"We cannot apply the English decisions in the matter of construction of the provisions of the Indian Act, particularly when they have received an authoritative interpretation from this court. In this view, it is not necessary to consider further English decisions cited by learned counsel for the respondent in support of his contention. Before a Division Bench of the Allahabad High Court in *Commissioner of Income-tax v. Kalicharan Jagan Nath*<sup>9</sup>, when a similar question arose, learned counsel appearing for the revenue relied upon the said English decisions, but the High Court, rightly, refused to act on them on the ground that they were not relevant in interpreting Section 4 of the Indian Income-tax Act."

13. In our view, unless the amount of compensation actually becomes payable or enforceable, it cannot be said to accrue or deemed to accrue. On the date when the Collector awarded the compensation, it is only that amount which had accrued or deemed to accrue, whether in fact paid or not. But by no stretch of the words in Section 4(1)(b)(i), could it be said that the right to enhanced compensation, which has not yet been accepted by the proper forum, namely, the court, has also become payable on the date when the original compensation became payable, for being included in that year of assessment. The enhanced compensation accrues only when it becomes

payable, i.e., when the court accepts the claim. As has been stated earlier, a mere claim by the assessee, after taking of possession of the land, at a particular rate or for a certain sum is not compensation. It must not be forgotten that, even if a court has awarded enhanced compensation, there is a right of appeal by the Government to the High Court, and the High Court may either disallow that claim or reduce the compensation. As against that judgment, there is a further right of appeal to the Supreme Court. The assessee also can appeal against the insufficiency of the enhanced compensation. Can it be said that the final determination by the highest court of the compensation would entitle the Income-tax Officer, notwithstanding the period of limitation fixed under the Income-tax Act, to reopen the assessment in which he had included the initial compensation awarded by the Collector and recompute the entire income on the basis of the final compensation? We do not think there can be any justification for such a proposition. On a proper construction of the terms "accrue" or "arise", we are of the view that such an interpretation cannot be placed. The interpretation given by us does not affect the interests of the revenue. At the same time, it safeguards the assessee and prevents harassment. To hold otherwise would be contrary to the provisions of law.

14. *In Commissioner of Income-tax v. Jai Prakash Om Prakash Co. Ltd.*<sup>10</sup>, . a Bench of the Punjab High Court was considering the point of time at which the amount claimed in a suit filed in the District Court, which was decreed, accrued or arose. There the assessee-company entered into a contract with Bharat Company for sale of mustard teeps, but the Bharat Company cancelled the transaction before the due date. The assessee sent a telegram to the Bharat Company to the effect that if the latter did not within 4 hours accept the settlement of the bargain at Rs. 16-14-6 a maund, it would presume that the latter had accepted the settlement, but there was no response to the telegram. This led to a suit by the assessee in the District Court against the Bharat Company for recovery of a sum of Rs. 73,820-12-0 (after adjusting a sum of Rs. 20,000 odd due from the assessee to the Bharat Company on account of some earlier transactions). This suit was decreed by the District Judge on 17/27th of February, 1954, against which an appeal was pending in the High Court. In the return filed by the assessee for the assessment year 1953-54 for which the accounting year was 1952-53, he appended a note in which he stated that there is a profit of Rs. 1,09,072 in the account of Bharat Co. Ltd., but that the company did not admit its liability, that the assessee had filed a suit for Rs. 75,000 after adjusting Rs. 34,072 received by the assessee, that unless the suit was decided, the exact amount of profit cannot be determined until the liability is admitted by the company, and that the exact profit will be shown when the same is determined by the civil court. The method of accounting employed by the assessee was on the mercantile basis. The Income-tax Officer included the sum of Rs. 94,000 as income which had accrued in the assessment year 1953-54, against which an appeal was preferred to the Appellate Assistant Commissioner, who confirmed the order of the Income-tax Officer. The Appellate Tribunal, however, accepted the assessee's contention and

held that the amount cannot be included as the income had not yet accrued. Mahajan J., with whom Khosla C.J. agreed in a separate judgment, observed at page 722 :

"The scheme of the Act would show that only those sums are taxable which accrue as income, i.e., they must" actually accrue or arise. No amount can be said to accrue unless it is actually due. Claim to an amount is not tantamount to the amount being due or, in other words, that the amount has accrued. In the instant case the very foundation of the claim is in jeopardy. If the appeal goes against the assessee, then nothing would be due. It is only if it goes in his favour that the amount will accrue."

15. Khosla C. J., also at page 723 said :

". . . . the profit was not actual, it had not accrued and was merely being claimed, the claim was being hotly contested and is still sub judice. That being so, the profit is nothing more than a notional figure which the assessee hopes to get."

16. A Bench of the Mysore High Court in *Commissioner of Income-tax v. Sampangiramaiah*<sup>11</sup>, were considering a case under the Land Acquisition Act. There the assessee's land was taken possession of in February, 1949. The compensation awarded by the Land Acquisition Officer was enhanced by the District Judge by a decree passed on 28th February, 1951, and was further enhanced by the High Court, and a sum of Rs. 1,15,000 representing the value of the land and Rs. 87,265 representing interest on that sum from the date on which delivery of possession was taken up to the date of payment, was paid to the assessee on October 21, 1961. The department assessed income-tax on the entire sum of Rs. 87,265 in the assessment year 1962-63. The Tribunal held that the interest that was payable to the assessee in each successive year accrued in that year and was liable to be assessed in that year itself and assessment of that interest cannot be postponed till the date on which the interest became ascertained or when the interest was actually paid to the assessee. The High Court, on a reference, agreed with the view of the Tribunal. Somnath Iyer J., after stating that the right to no part of the interest was born until the Land Acquisition Officer made his arithmetic after the Supreme Court disposed of the appeals, cannot have the support of reason, observed at page 163 :

"There was thus a complete acquisition of the right to recover the accumulated interest on the amount awarded by the Land Acquisition Officer when possession was taken and on the enhancement, when the appropriate decree made such enhancement and to subsequent interest so long as it ran but was not paid. Such interest became income which accrued in the year in which it became so recoverable within the meaning of Section 4(1)(b)(i) of the Income-tax Act, 1922, so long as that Act was in force, and of Section 5(1)(b) of the Income-tax Act, 1961, when that Act commenced to operate. The attribution of the whole of that interest to the year of receipt is

manifestly impossible."

17. A Bench of this Court to which one of us (the Chief Justice) was a party in *Sreeramamurty v. Commissioner of Income-tax*<sup>12</sup>, after a review of the case law, had, in a case where the Government did not admit the claim of the rice miller till after the accounting year had ended, held that it is only after the claim was admitted that the amount can be deemed to have accrued, because the assessee was maintaining the mercantile system of accounting. In coming to this conclusion, it was observed that the meaning of the word "accrue" or "arise" in Section 4(1)(b)(i) of the Income-tax Act cannot be extended so as to take in amounts received in a later year, though the receipt was not on the basis of a right accrued in an earlier year. It held, having regard to the several decisions cited therein, that the claim, notwithstanding the fact that it was made in the accounting year, did not arise or accrue in the accounting year so as to be included in that year.

18. In this view, our answer to the first question is in the affirmative and in favor of the department, as already indicated. Our answer to the second question is in the negative and in favour of the assessee. As the assessee substantially succeeds, it will have its costs. Advocate's fee Rs. 250.

#### Cases Referred.

- 1[1925] 1 I.T.C. 367, 376
- 2[1888] 21 Q.B.D. 52
- 3[1965] 55 I.T.R. 462, 470
- 4[1923] 13 T.C. 723
- 5[1927] 12 T.C. 927
- 6[1947] 29 T.C. 69 ; [1947] 1 All E.R. 650
- 7[1921] (sic) T.C. 382
- 8[1954] 35 T.C. 649
- 9[1961] 41 I.T.R. 40
- 10[1961] 41 I.T.R. 718
- 11[1968] 69 I.T.R. 159
- 12[1966] 1 A.L.T. 358

