

INCOME-TAX REFERENCE

Before D. K. Mahajan and Gopal Singh, JJ.

THE COMMISSIONER OF INCOME-TAX, PATIALA,—Applicant.

versus

DR. SHAM LAL NARULA, PATIALA,—Respondent.

Income Tax Reference No. 16 of 1969

January 6, 1971.

Income-Tax Act (XI of 1922)—Section 4(1)(b)(i)—Land Acquisition Act (I of 1894)—Sections 16, 17 and 34—Acquisition of land in 1951—Interest on compensation paid in the assessment year 1956-57—Receipt of such interest-income—Whether assessable in the year of receipt—Such interest-income—Whether accrues from year to year after acquisition.

Held, that under section 34 of Land Acquisition Act, 1894; the right to recover interest arises the moment the owner is deprived of his property under that Act. The reason is obvious. The owner of property after his dispossession under section 17 of the Act is deprived of the income from the same. This does not happen if the possession is taken under section 16 of the Act. It is for this reason that section 34 has made a special provision for payment of interest from the date he is deprived of possession without payment of compensation so that the interest on such compensation compensates him for the loss of income which would have accrued to him if the possession had been taken after making the award under section 16. Interest is only payable where an owner is deprived of his property and the payment of its compensation is deferred. Therefore, the benefit which he is to acquire from the property or land is benefit accruing every year which is compensated by way of interest under section 34. The interest is definitely accruing each year and is payable as such after the possession is taken from the owner. Hence where land is acquired in 1951, but interest on compensation is paid in assessment year 1956-57, the interest-income is not assessable in the year of receipt. Such interest becomes income in the year in which it becomes so recoverable within the meaning of section 4(1)(b)(i) of the Income-tax Act, 1922, and as such only the interest referable to the relevant assessment year can be brought to tax in that assessment year.

(Para 4 and 5)

Income-tax Reference under section 66(1) of the Income-tax Act, 1922 made to this Court by the Income-tax Appellate Tribunal (Delhi Bench) vide his letter No. R.A. 1533/67-68, dated 6th February, 1969, for opinion in case R.A. No. 1533 of 1967-68 on the following question of law arising out of I.T.A. No. 5276 of 1957-58 for assessment year 1956-57:—

“Whether on the facts and in the circumstances of the case the Tribunal was right in law in deleting the amount of Rs. 42,577.50 P. out of Rs. 48,660 from the assessment for the assessment year 1956-57?”

D. N. AWASTHY AND BALWANT SINGH GUPTA, ADVOCATES, for the applicant.

ATMA RAM AND JAGMOHAN SINGH, ADVOCATES, for the respondent.

JUDGMENT

MAHAJAN, J.—(1) The Income-tax Appellate Tribunal, Delhi Bench 'A', at the instance of the Department, has referred the following question of law for our opinion:—

“Whether on the facts and in the circumstances of the case the Tribunal was right in law in deleting the amount of Rs. 42,577.50 P. out of Rs. 48,660 from the assessment for the assessment year 1956-57 ?”

(2) The assessee, a Hindu undivided family, owned land. Land measuring 40 Bighas and 11 Biswas was acquired by the State Government. The notification acquiring the land was issued on 21st of June, 1950. This notification was issued under section 9 of the Patiala Land Acquisition Act of 1895 Bk. and Patiala Land Acquisition Act of 2006 Bk. Both these Acts were replaced and the proceedings for the acquisition were finalised under the Indian Act. Later on, a notification was issued on the 11th October, 1953, withdrawing the acquisition proceedings. The validity of this notification was challenged by the assessee and this notification was quashed by the Pepsu High Court on 14th of February, 1955. On the 15th October, 1951, the assessee was deprived of possession of the land. The Collector made his award on 30th of September, 1955. The assessee was dissatisfied with this award and applied for reference under section 18 of the Land Acquisition Act to the District Judge. The learned District Judge enhanced the compensation and excepting by way of historical importance, this fact has no material bearing on this case. In the ultimate analysis, it was found that the assessee was due interest on the amount of compensation awarded to him to the tune of Rs. 48,660. This interest was paid to him in the year previous to the assessment year 1956-57. The Department proceeded to assess this interest to income-tax. The assessee claimed that the interest could not be taxed to income-tax at all. He failed in his contention right up to the Supreme Court. After the decision of the Supreme Court, the assessee raised the contention that the entire interest could not be assessed in the year 1956-57. It had to be spread over the various years for which it had accrued due. This contention did not find favour with the Income-tax Officer and so also with the Appellate Assistant Commissioner in appeal. However, on appeal to the Tribunal, the Tribunal held that only the interest referable to the

The Commissioner of Income-tax, Patiala v. Dr. Sham Lal Narula, Patiala
(Mahajan, J.)

relevant assessment year could be brought to tax. The relevant part of the decision of the Tribunal is as follows:—

“On the above facts the question for determination is as to whether the entire interest accrued to the assessee during the previous year or only part thereof. In this connection reference may be made to the observations of their Lordships of the Bombay High Court in the case of *Commissioner of Income-tax, Bombay City II v. Associated Commercial Corporation* (1). Their Lordships have quoted with approval the observations of the Punjab High Court in the case of *Commissioner of Income-tax v. Jai Parkash Om Parkash and Co. Ltd.* (2) to the following effect :—

‘The scheme of the Income-tax Act showed that only those sums were taxable which accrued as income, i.e., they must have actually accrued or arisen. No amount could be said to accrue unless it was actually due. A claim to an amount was not tantamount to the amount being due or having accrued.’

Their Lordships after quoting the above observations of the Punjab High Court have at page 18 observed as follows:—

‘The learned Judges observed in that case that the foundation of the claim was in jeopardy at the time when the claim was said to have accrued to the assessee, and included in his taxable income and they pointed out that it was only when the claim was no longer in jeopardy as a result of having been decided in his favour that the amount could be said to have accrued to the assessee. In our opinion, a profit could be said to have accrued or a liability or loss could be said to have been incurred only when the profit is either actually due or the liability becomes enforceable. A mere claim to a profit or to a liability is not sufficient to make the profit to accrue or the liability to be incurred for the purposes of the Income-tax Act. In the case in *Commissioner of Income-tax v. Mathulal Buldeo Prashad* (3), which was a case of liability, the same principle

(1) (1963) 48 I.T.R. 1

(2) 41 I.T.R. 718.

(3) 42 I.T.R. 517.

has been laid down by the Allahabad High Court. The learned Judges held that a mere assertion of a claim would not be sufficient to hold that the amount claimed had accrued. It is only at the stage when the claim was found to be correct by the arbitrator in that case that the claim could be said to have become an actual enforceable liability against the assessee. An enforceable liability would be deemed to have come into existence when and only when it was determined and fixed by the arbitrator.'

At page 19 their Lordships have quoted the observations of their Lordships of the Supreme Court to the following effect :—

'But in order that the income can be said to have accrued to or earned by the assessee it is not only necessary that the assessee must have contributed to its accruing or arising by rendering services or otherwise, but he must have created a debt in his favour. A debt must have come into existence and he must have acquired a right to receive the payment. Unless and until his contribution or parenthood is effective in bringing into existence a debt or a right to receive the payment or in other words a *debitum in praesenti, solvendum in futuro* it cannot be said that any income has accrued to him.'

In the instant case, it would be noted that the assessee's claim was very much in jeopardy, inasmuch as the Government had on 14th October, 1953, intimated to the assessee their decision to withdraw from the acquisition. It was only the judgment of the High Court passed on 14th February, 1955, quashing the Government notice to withdraw from the acquisition that finally settled the assessee's right to receive the compensation as also the interest thereon which is now in dispute before us. It would thus appear that the right to receive the interest was finalised and determined only as a result of the decision of the High Court on 14th February, 1955. Since the enforceable liability was determined only as a result of the order of the High Court, it would appear that the income can be held to have accrued

The Commissioner of Income-tax, Patiala v. Dr. Sham Lal Narula, Patiala
(Mahajan, J.)

only during the previous year ending on 31st March, 1955. Similar is the view taken by their Lordships of the Allahabad High Court who have in the case of *Commissioner of Income-tax v. Kalicharan Jagannath* (4), held that income accrues or arises only when the right to receive the payment comes into existence. It has already been noted above that the assessee's right to receive that payment in dispute was determined only by the judgment of the High Court on 14th February, 1955. The interest income would, therefore, be held to have arisen or accrued to the assessee only on 14th February, 1955. Thereafter, interest accrued to the assessee on the amount determined to be payable as compensation. It would thus appear that interest to the tune of Rs. 42,577.50 being interest due for the account years 1951-52 to 1954-55 accrued in the previous year ending 31st March, 1955 and it is only interest of Rs. 6,082.50 pertaining to the period after 1st April, 1955, that accrued and was received by the assessee during the previous year. I would, therefore, agree that only the interest of Rs. 6,082.50 is to be included in the total income of the previous year and the balance is to be deleted."

(3) Against this decision, the Department applied for a reference under section 66(1) of the Income-tax Act, 1922, and that is how the question of law already stated has been referred for our opinion:

(4) Mr. Awasthy, learned counsel for the Department, has very strenuously contended that the decision of the Tribunal is incorrect. The learned counsel mainly relies upon the decision of the Andhra Pradesh High Court in *Khan Bahadur Ahmed Alladin and Sons v. Commissioner of Income-tax* (5). We have gone through this decision and find that it has no applicability to the facts of the present case. The main stress of the learned counsel's argument was that the right of compensation under the Land Acquisition Act is an inchoate right until an award is given, but this argument cannot be accepted so far as the question of interest is concerned because section 34 of the Land Acquisition Act does not leave the right to interest inchoate. In

(4) (1961) 41 I.T.R. 40.

(5) 74 I.T.R. 651.

fact, the decision of the Tribunal is in line with the decision of the Mysore High Court in *Commissioner of Income-tax, Mysore v. V. Sampangiramaiah* (6). The facts of the Mysore case are more or less *pari materia* with the facts in the present case. It is not necessary for us to re-state the reasons that prevailed with the learned Judges of the Mysore High Court. We have for facility of reference reproduced the relevant extract from their judgment:—

“But the question in this reference is, whether the right to the whole of the interest accrued only when it was paid. If it did not, and if the interest in respect of the period which commenced on April 1, 1961, and expired on October 12, 1961, was all that accrued during the relevant preceding year and the interest in respect of the antecedent period had accrued earlier, earlier whatever may be the points of time when there was such accrual, the Appellate Tribunal's view would be irreproachable.

Now, when possession was taken by the Land Acquisition Officer, he became liable to pay interest until the amount awarded by him was paid, and the assessee acquired the right to recover it from him. The direction of the District Judge for the payment of interest on the enhanced compensation, which, his decree made on February 28, 1951, incorporated produced the right to recover such interest at least on the date of that decree. Then again, when compensation was further enhanced by the former High Court of Mysore which made a similar direction for the payment of interest on such enhanced compensation, all that interest which that amount so earned from February 19, 1949, became immediately due and payable under an executable decree.

It is difficult to understand how the pendency of the appeal before the Supreme Court could arrest the accrual of that income. It did not. It is admitted that during the pendency of the appeals before the Supreme Court, there was no stay of execution. Even if there was, its impact on accrual is debatable.

The Commissioner of Income-tax, Patiala v. Dr. Sham Lal Narula, Patiala
(Mahajan, J.)

So, the premise 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.

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.

The omission by the assessee to include the interest which had so accrued to him in the returns of the earlier years cannot yield the deduction that he chose to treat the interest as the income of the year in which he received it. Indeed, no such theory was evolved at any stage. On the contrary, it should be remembered that the contention of the assessee has all along been that no part of the interest was a revenue receipt and it is not unintelligible that it is due to that reason that there was an omission to disclose the interest which had accrued due when he produced the returns for the earlier years.

The principle on which the finding of the Tribunal rested was that which emerges from the decision of the Supreme Court in *E. D. Sasson and Company Ltd. v. Commissioner of Income-tax* (7) in which it was observed :

'The computation of the profits whenever it may take place cannot possibly be allowed to suspend their accrual...'

'What has however got to be determined is whether the income, profits or gains accrued to the assessee and in order that the same may accrue to him it is necessary that he must

have acquired a right to receive the same or that a right to the income, profits or gains has become vested in him though its valuation may be postponed or though its materialisation may depend on the contingency that the making up of the accounts would show income, profits or gains'

This enunciation continues to be the law and stands in no way impaired by the subsequent decision in *Commissioner of Income-tax v. A. Gajapathy Naidu* (8), on which Mr. Rajasekhara Murthy depends.

If this was the principle by the application of which the Tribunal deduced its conclusion, very little could be said in criticism of the attribution made by it.

But Mr. Rajasekhara Murthy asks us to say that even if the right to interest had accrued to the assessee periodically during the many years which preceded the assessment year 1962-63, so long as the assessee did not maintain his accounts on the mercantile basis, the interest received by him during the previous year relating to the assessment year 1962-63, could be taxed during that assessment year. In support of this argument, he depended upon the observations in *Gajapathy Naidu's case* (8), in which there was an explanation of the familiar rule that income is taxable when it accrues or is earned, if the assessee's accounts are maintained on the mercantile basis, and when it is received, if the method of accounting is the cash system. But this elucidation does not take the department far enough. The mercantile system which, when regularly employed, credits income immediately after it becomes due and recoverable, dispenses, in a proper case, with further proof, that it then accrued, while the cash system which displays the choice of the assessee to treat the income as having arisen when it was received, regulates computation accordingly. And in the case before us, in which the Appellate Tribunal did not find that the method of accounting employed was the one or the other, the income became taxable when it became legally due and recoverable, for, it is then that it accrued.

The Commissioner of Income-tax, Patiala v. Dr. Sham Lal Narula, Patiala
(Mahajan, J.)

That being so, we must answer the question referred to us in favour of the assessee, and our answer is that the Appellate Tribunal was right in holding that the entire interest amount of Rs. 87,265 was not assessable in the assessment year 1962-63 and that only the proportionate interest referable to the assessment year 1962-63 was assessable in that year."

(5) We entirely agree with the above observations. However, we wish to stress the provisions of section 34 of the Land Acquisition Act. These provisions were noticed by the learned Judges of the Mysore High Court, but there is an additional reason which we must mention in support of the conclusion at which the learned Judges of the Mysore High Court arrived at for the view which has prevailed with the Tribunal. Under section 34, the right to recover interest arises the moment the owner is deprived of his property under the Land Acquisition Act. The rate at which he is entitled to interest is also specified. The reason for this is obvious. The owner of property after his dispossession under section 17 of the Land Acquisition Act is deprived of the income from the same. This does not happen if the possession is taken under section 16 of the said Act. It is for this reason that section 34 made a special provision for payment of interest from the date he is deprived of possession without payment of compensation so that the interest on such compensation, compensates him for the loss of income which would have accrued to him if the possession had been taken after making the award under section 16 and after payment of compensation. Interest is only payable where an owner is deprived of his property and the payment of its compensation is deferred. Therefore, it is obvious that the benefit which he was to acquire from the property or land was benefit accruing every year which is compensated by way of interest under section 34. If this is kept in view there is no difficulty in understanding the decision of the Mysore High Court. The interest is definitely accruing each year and is payable as such after the possession is taken from the owner.

(6) The other contention of Mr. Awasthy is that admittedly in this case no account was kept. This argument is wholly futile for the reason that here the owner was deprived of his property and he was not doing the business of buying and selling property and, therefore, there was no question of his keeping any account. All he was

interested in was to receive the compensation and as a consequence of the delayed payment of compensation he became entitled to interest under section 34.

(7) It is further maintained that in the case of the assessee the interest had to be brought to tax on receipt basis because there was no method of accounting. As already pointed out, there is no question of an owner of property who has been deprived of it under the Land Acquisition Act maintaining any accounts, unless of course dealing with property was his business. But for section 34, the assessee would not be entitled to relief which the Tribunal gave. It is only on the basis of this provision that he is entitled to interest. The view we have taken finds ample support from the decision of the Supreme Court in *E. D. Sassoon and Company Ltd. v. The Commissioner of Income-tax, Bombay City* (9).

(8) It will also be profitable to refer to the decision of this Court in *Commissioner of Income-tax, Punjab v. Sham Lal Narula* (10), particularly to the following observations at page 529 of the report:—

“The payment under section 34 cannot be said to be without apparent cause, or in any unaccountable manner, or as a mere coincidence, or not designedly brought about in the sense of being unexpected, unforeseen or without regularity. The word ‘casual’ is an antonym for ‘regular’ in the sense that something happens at uncertain times. In this sense payment under section 34 is not casual. Once payment of the compensation under section 23 is withheld after the taking of possession of the land acquired, the payment of interest at 4 per cent per annum becomes not casually, but regularly and recurrently payable. I cannot, therefore, persuade myself to treat the receipt as exempt from tax on the ground that it is ‘of a casual and non-recurring nature’.”

(9) For the reasons recorded above, we answer the question referred to us in the affirmative, that is, against the Department and in favour of the assessee. There will be no order as to costs.

GOPAL SINGH, J.—I agree.

B. S. G.

(9) 1955 S.C.R. 313.

(10) 50 I.T.R. 513.