IN THE HIGH COURT OF JUDICATURE AT MADRAS

DATED : 12.09.2022

CORAM :

THE HON'BLE MR. JUSTICE S.VAIDYANATHAN
AND
THE HON'BLE MR. JUSTICE C.SARAVANAN

T.C.A.No.1114 of 2009

M/s.UC MAS Mental Arithmetic (India) Pvt. Ltd.
Rep. by its Managing Director Mr.Basheer Ahmad,
A-1, 1857, 13th Main Road, VI Avenue,
Anna Nagar,
Chennai 600 040. .. Appellant

Versus

The Assistant Commissioner of Income Tax
Company Circle III(3), Chennai. ..Respondent

Tax Case Appeal filed under Section 260-A of the Income Tax Act, 1961 against the order of the Income Tax Appellate Tribunal, 'D' Bench, Chennai dated 20.02.2009 passed in I.T.A.No.750(MDS)/08.

For Appellant : Mr. TC.A.Ramanujam

For Respondent : Mr.V.Pushpa

J U D G M E N T

S.VAIDYANATHAN,J
and
C.SARAVANAN, J

This Tax Case Appeal has been filed by the Assessee, calling in question the order dated 20.02.2009 passed by the Income Tax Appellate Tribunal, Madras 'B' Bench, in I.T.A.No.750/(MDS)/08 relating to the Assessment Year 2004-05.

2. By order dated 10.11.2009, TCA No.1114 of 2009 was admitted on the following substantial question of law :-

> *"Whether in the facts and in the circumstances of the case, the income tax Appellate Tribunal is justified in allowing the commission paid to the Managing Director for the assessment year 2004-2005 in the assessment of the appellant company when the appellant company is following mercantile system of accounting and such method of accounting has been accepted by the department in all the other years?"*

3. The facts in nutshell placed before this Court are as follows:

(i) The Appellant Company /Assessee was engaged in the business of imparting mental arithmetic training through images and mental reckoning methods for fast and accurate calculations. For the Assessment Year 2004-2005, the Appellant claimed a deduction of Rs.30,45,396/- being the royalty paid to the Franchisor under the Master Franchise Agreement dated 16.07.2002. The Assessing Officer disallowed the claim of the Appellant on the basis that the payments were capital expenditure and came to the conclusion that the Appellant acquired a benefit of enduring nature and treated the payment of Rs.30,45,396/- as capital expenditure and also allowed depreciation under Section 32 of the Income Tax Act, 1961. Aggrieved over the same, the Appellant has preferred an Appeal before the Commissioner of Income Tax (Appeals)-III, Chennai and the said Authority taking note of the fact that for the previous Assessment Year, the Assessee had the benefit of similar payment, which was not treated as Capital Asset has allowed the Appeal vide order dated 29.01.2008.

(ii) Being aggrieved over the same, the Respondent preferred an Appeal before the Income Tax Appellate Tribunal (for brevity 'the Tribunal') and the Tribunal vide order dated 20.02.2009 has allowed the Appeal insofar as it relates to the payment to the Managing Director, while the royalty payments were allowed as revenue expenditure. Being aggrieved, the Assessee has preferred this Appeal.

2. The narrow issue involved in this case is whether or not the payment

made to the Managing Director to the tune of Rs.30 lakhs is to be treated as deductible expenditure on the basis of the resolution dated 11.12.2003, which permits to increase the remuneration payable to the Managing Director from 01.04.2003 and to pass commission after approval of the members in the ensuing Annual General Meeting, which took place on 30.09.2004, wherein the earlier resolution was ratified. The Assessment Officer did not accept the claim of the Assesee for the Assessment Year 2005-2006 as the liability arose from 2005-2006. The Tribunal, on scrutiny of the order of Assessing Officer held as follows:-

> "*10. As regards the contention that the department had accepted the assessee's method of accounting in earlier period we find that there is no discussion on this topic in the order for the earlier assessment year produced before us. It cannot be said that the Assessing Officer had formed any opinion on the system being followed by the assessee in earlier period.*
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> *11. In the background of the aforesaid discussion and in the light of the fact that in the individual case of the payee it was argued that the right to receive the payment arose only upon the approval by the shareholders in the annual general meeting, in out opinion, the payment of enhanced commission became due only upon the approval by the company in the annual general meeting. We, therefore, find force in the arguments advanced by the Revenue in this regard and accordingly this ground is decided in favour of the Revenue.*"

3. The main contention of the learned counsel for the Appellant is that the

Tribunal is not justified in disallowing the Commission paid to the Managing Director for the Assement Year 2004-2005. It is further contended that when the mercantile system of accounting is permissible in the trade business, which was also accepted by the Revenue in the earlier litigation held before the Apex Court in the case of ***Metal Box Company of India Ltd., Vs. Their Workmen*** reported in (***1969) 73 ITR 53 (SC),*** *wherein it was held as follows:*

> *"Accrued but discharged liability must be allowed under mercantile system: in the case of an assessee maintaining his accounts on mercantile system, a liability already accrued, tough to be discharged at a future date, would be a proper deduction while working out the profit and gains of his business, regard being had to be accepted principles of commercial practice and accountancy, it is not as if such deduction is permissible only in case of amounts actually expended or paid. Just as actual receipts as well as those accrued due are brought in for income tax assessment, so also liabilities accrued due would be taken into account while working out the profits and gains of the business."*

4. The learned counsel appearing for the Respondent would submit that the Tribunal has rightly held that the expenditure incurred can be treated as Revenue expenditure and not as capital expenditure and therefore the order of the Tribunal does not warrant interference.

5. Heard the learned counsel appearing for the Appellant as well as the

learned standing counsel appearing for the Respondent.

6. On a careful perusal of the order of the Assessment Officer, we are of the view that the methodology adopted by the Revenue is perfectly correct for the simple reason that it is not disputed that the amount has been shown as expenditure and that the payment has been made to the Managing Director. However, the amount has been received by the beneficiary only for the subsequent Assessment Year, which does not mean that as long as the Appellant has not shown the payment in the Books of Accounts in respect of liability, it cannot be stated that the expenditure was incurred during 2004-2005 as such expenditure would be ratified only after Board's meeting.

7. In view of the above,we have no other option, but to dismiss this Appeal. Accordingly, this Tax Case Appeal is dismissed and the question of law as framed is answered against the Assessee and in favour of the Revenue.

In the result, this Tax Case Appeal is dismissed. No costs.

[S.V.N., J.] [C.S.N., J.]
12.09.2022

Internet : Yes
Index : Yes / No

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To

1.The Income Tax Appellate Tribunal
Chennai 'D' Bench.

2.The Assistant Commissioner of Income Tax
Company Circle III(3), Chennai.

3. Income Tax Officer, Company Ward III (1),
Chennai-34.

S.VAIDYANATHAN, J.
and
C.SARAVANAN, J.

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