

INCOME TAX : Where assessee set-off/adjusted sales tax liability that arose at time of purchase of raw materials against sales tax collected at time of sale of finished goods, such amount of sales tax liability set off/adjusted, by legal fiction, was deemed to be an actual payment of tax liability and was deductible under section 43B

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[2021] 132 taxmann.com 174 (Bombay)

HIGH COURT OF BOMBAY

Merck Ltd.

v.

Dy. Commissioner of Income-tax, Range-3, Mumbai*

K.R. SHRIRAM AND M.S. KARNIK, JJ.

IT APPEAL NO. 208 OF 2003

SEPTEMBER 16, 2021

Section 43B of the Income-tax Act, 1961 - Business disallowance - Certain deductions to be allowed only on actual payment (Taxes) - Assessment year 1988-89 - Whether where assessee had set-off/adjusted sales tax liability that arose at time of purchase of raw materials against sales tax collected at time of sale of finished goods, such amount of sales tax liability set off/adjusted, by legal fiction, was deemed to be an actual payment of tax liability and was deductible under section 43B - Held, yes [Paras 6 and 7] [In favour of assessee]

Words and Phrases: Words 'actually paid by him' as occurring in section 43B of the Income-tax Act, 1961

CASE REVIEW

CIT v. National Standard Duncan Ltd. [2004] 134 Taxman 563/[2003] 260 ITR 97 (Cal.) (para 6) followed.

CASES REFERRED TO

CIT v. National Standard Duncan Ltd. [2004] 134 Taxman 563/[2003] 260 ITR 97 (Cal.) (para 6).

Ms. Arati Vissanji and S.J. Mehta for the Appellant. **Suresh Kumar** for the Respondent.

JUDGMENT

K.R. Shriram, J. - This pertains to Assessment Year 1988-89. Appellant had claimed a sum of Rs. 7,06,590/- being sales tax set off as deduction under section 43B of the Income-tax Act, 1961 (the Act). According to appellant, the sales tax set off represents that part of the purchase tax paid by appellant on purchase of raw materials and packing materials, which is allowed to be retained by it as the materials purchased are consumed in the manufacture of finished goods which are again liable to sales tax. This means that the said amount is not payable to the sales tax authorities at the time of paying the sales tax on the sale of finished goods by appellant. According to appellant, the fact that they are entitled to claim the set off would mean that a legal fiction is created to the effect that this amount of Rs. 7,06,590/- be treated to have been paid as a tax liability deductible under section 43B of the Act.

This was disallowed by the Assessing Officer by an order dated 21st February 1991.

An appeal was preferred by petitioner under section 216 of the Act. The CIT(A) by an order dated 8th July 1992 upheld the disallowance of Rs. 7,06,590/- by the Assessing Officer. Petitioner challenged the order of CIT(A) before ITAT. ITAT dismissed this issue in its order dated 1st January 2002 as not pressed for.

Petitioner filed a miscellaneous application relating to this disallowance of Rs. 7,06,590/- under section 43B of the Act, which also came to be rejected by ITAT *vide* its order dated 7th November 2002 without a hearing.

2. The fact that appellant was entitled to a set off or adjustment made on the sales tax amount, is not disputed. According to Mr. Suresh Kumar, this amount of Rs. 7,06,590/- was never paid but was retained by appellant and even if any adjustment or set off is claimed, there was no actual payment and unless there is actual payment, section 43B of the Act does not come into play and, therefore, appellant cannot claim any benefit thereof.

The only question to be decided therefore is, whether the expression "actually paid by him" in Section 43B also included the amount which has been set off or adjusted?

3. By an order dated 7th October 2004, this court was pleased to admit the appeal as it was satisfied that the case involved a substantial question of law. The court was pleased to frame the following two questions of law:

"1. Whether on the facts and circumstances of the case, the conclusion of the Tribunal that the appellant had not pressed the ground relating to the disallowance of the sales tax set off Rs. 7,06,590/- under section 43B for the assessment year 1988-89 is correct?

2. Whether on the facts and circumstances of the case and in law, the claim for sales tax set off of Rs. 7,06,590/- for the assessment year 1988-89 has been rightly disallowed under section 43B of the Act ?"

4. As regards the first question, Mr. Suresh Kumar submitted that since this point was not pressed for by appellant before the Tribunal, the court should not even consider the second question. We are at final hearing stage. In question no. 1, the court has recorded whether the conclusion of the Tribunal that appellant had not pressed the ground relating to the disallowance under section 43B of the Income-tax Act (hereinafter referred to as the said Act), is correct? Therefore, the court was aware that it was respondents' case that it was not pressed for. Notwithstanding that the court still framed question no. 2. Therefore, we are inclined to answer question no. 2.

5. Section 43B reads as under:

"43B:- 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)

(c)

(d)

(da)

(e)

(f)

(g)

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.

....."

6. Section 43B of the Act, therefore, provides for deduction notwithstanding anything contained in any other provision of the Act in respect of 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. According to respondents it shall be allowed provided the sum is actually paid. As noted earlier the amount of Rs. 7,06,590/- has been set off because appellant was entitled to set off this amount. In our view, the amount of Rs. 7,06,590/- which has since been liability due to be paid having been adjusted, is a deemed payment amounting to actual payment within the meaning of section 43B of the Act. Since the law permits appellant to set off or adjust the sales tax already paid at the time of purchase of raw materials against the sales tax collected at the time of sale of finished goods, the assessee has retained the sales tax amount which has already paid and claimed a set off. In fact to the extent of the sales tax paid on the raw materials, the assessee has actually been reimbursed to that extent by the sales tax collected at the sale of the finished product. Therefore, it is presumed to be a deemed payment within the time to be included in the relevant assessment. Since the assessee was entitled to adjustment or set off, the amount of Rs. 7,06,590/- is a liability adjusted deeming actual payment by legal fiction. This adjustment, by legal fiction, is deemed to be an actual payment of the tax liability and is deductible under section 43B of the Act. We find support for this view in a judgment of the Calcutta High Court in *CIT v. National Standard Duncan Ltd.* [2004] 134 Taxman 563/[2003] 260 ITR 97 where the court held as under:

'Section 43B of the 1961 Act provides for deduction notwithstanding anything contained in any other provision of the 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 . . ." This section is qualified by one *Explanation*. The *Explanation* explains that where deduction is allowed on the liability to pay in the assessment for the previous year when the liability was incurred, the assessee shall not be entitled to deduction in the assessment for the previous year in which the amount is actually paid. The scheme of the section makes it clear that the Legislature has left nothing unambiguous to express its intention that such deduction is allowed once, either on the actual payment or on the liability, as the case may be.

"A part of the sales tax collected has since been paid. The balance has been sought for being adjusted or being set off under rule 41D read with rule 45(3) of the Bombay Sales Tax Rules. Therefore, it is to be presumed to be a deemed payment within the time to be included in the relevant assessment. The allowance is allowed in respect of the sales tax payable by the assessee, which is qualified by the *Explanation* to Section 43B of the Income-tax Act to mean to have been actually paid or incurred. That the liability was incurred is not in dispute. In this case it has not been actually paid, but was sought to be adjusted or set off against payment of sales tax by the assessee on its purchase of raw material used for the product against which the sales tax has since been collected by the assessee on sale of the product concerned."

Now it is to be seen whether the set off or adjustment amounts to deemed payment. In other words,

whether this deemed payment is a payment of the liability contemplated under section 43B of the Income-tax Act. Rule 41D of the Bombay Sales Tax Rules allowed incentive by way of exemption of sales tax to the extent of payment of sales tax on purchase of raw material used for the product. Rule 45(3) entitles the assessee to adjust or set off the amount in the return itself. It is a provision parallel to sections 199 and 245 of the Income-tax Act creating a legal fiction. Therefore, this sum, which is subject to adjustment or set off, is a liability adjusted deeming actual payment by legal fiction. The Sales Tax Rules have allowed an incentive by way of adjustment of sales tax or in other words, the liability is being adjusted as actual payment. Section 43B of the Income-tax Act allows deduction on tax payable by the assessee. When the assessee purchases raw materials, it is liable to pay purchase tax on the purchase. An equivalent of this amount is adjusted towards the liability on the sale of the product produced out of the raw materials purchased. This adjustment, by legal fiction, is deemed to be an actual payment of the tax liability. Admittedly, this amount is a tax payable. If it is a tax liability on being set off or adjusted, deemed actual payment by legal fiction, it is deductible under section 43B of the Act.'

7. Therefore, in the facts and circumstances of the case, the disallowance for sales tax set off of Rs. 7,06,590/- for Assessment Year 1988-89 was not correct. Question no. 2 is answered accordingly.

8. Appeal disposed with no order as to costs.

Tanvi

*In favour of assessee.