

आयकर अपीलिय अधिकरण पुणे न्यायपीठ "बी" पुणे में
**IN THE INCOME TAX APPELLATE TRIBUNAL
PUNE BENCH "B", PUNE**

सुश्री सुषमा चावला, न्यायिक सदस्य एवं श्री डी. करुणाकरा राव, लेखा सदस्य के समक्ष
BEFORE MS. SUSHMA CHOWLA, JM AND SHRI D. KARUNAKARA RAO, AM

आयकर अपील सं. / **ITA No.377/PUN/2016**
निर्धारण वर्ष / **Assessment Year : 2010-11**

Dy. Commissioner of Income-tax,
Circle-7, Pune

.... अपीलार्थी/Appellant

Vs.

M/s. Tranter India Pvt. Ltd.,
Gat No.127 & 128,
Dhingrajwadi, Taluka Shiruru,
Off Pune Nagar Road,
Pune – 412 208
PAN : AAFC4598P

.... प्रत्यर्थी / Respondent

आयकर अपील सं. / **ITA No.478/PUN/2016**
निर्धारण वर्ष / **Assessment Year : 2010-11**

M/s. Tranter India Pvt. Ltd.,
Gat No.127 & 128,
Dhingrajwadi, Taluka Shirur,
Off Pune Nagar Road,
Pune – 412 208
PAN : AAFC4598P

.... अपीलार्थी/Appellant

Vs.

Dy. Commissioner of Income-tax,
Circle-7, Pune

.... प्रत्यर्थी / Respondent

Assessee by : Shri Manoj Solanki
Revenue by : Shri Prashant Gadekar

सुनवाई की तारीख / Date of Hearing : 07.02.2018	घोषणा की तारीख / Date of Pronouncement: 09.02.2018
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आदेश / ORDER

PER D. KARUNAKARA RAO, AM :

These are the cross appeals filed by Revenue as well as the Assessee in connection with the finding of the CIT(A) vide his order dated 22-12-2015 for the Assessment Year 2010-11.

2. Briefly stated, general facts relating to the assessee's case include that the assessee is engaged in the manufacturing and sale of various types of Heat Exchangers. Assessee filed the return of income for the A.Y. 2010-11 declaring total income of Rs.3.80 Crores (Rounded off). At the end of the assessment proceedings u/s.143(3) of the Act, the assessed income was determined at Rs.5.16 Crores (Rounded off) after making certain additions/disallowances. The disallowances on account of "Bad debts" and "Provision of warranty" are two of them. In the First Appellate proceedings, the CIT(A) granted relief to the assessee on the addition relating to the "provision of warranty". Aggrieved with the same, the Revenue is in appeal on this issue. Further, regarding the "Bad debts", the CIT(A) confirmed the addition and decided against the assessee. Aggrieved with the said conclusion of the CIT(A), the Assessee is in appeal on this issue of Bad debts.

3. We shall now take up the appeal-wise adjudication in the following paragraphs.

ITA No.377/PUN/2016 – (By Revenue)

4. Grounds raised by the Revenue read as under :

"1. Whether on the facts and in the circumstances of case and in law, the Ld.CIT(A) was justified in allowing the provisions of warranty expenses of Rs.1,05,40,638/- as an allowable deduction u/s.37 of the Act?"

"2. Without prejudice to the above, whether on the facts and in the circumstances of the case, the Ld.CIT(A) erred in not restricting the allowance to Rs.17,37,265/- being actual warranty cost during the year as held by Hon'ble ITAT, Pune in the case of Kalyani Brakes Ltd. (ITA No.578 & 579/PN/09)?"

5. The only issue raised in the grounds extracted above relate to the provision of warranty. Assessee claimed expenses on this account amounting to Rs.1,05,40,638/- u/s.37 of the Act. Out of the above, actual utilisation out of the

provision was only Rs.17,37,265/-. It is the case of AO, like in other years, warranty provision created by the assessee does not match with the actual utilisation towards the warranty claims of the customers. Therefore, AO questioned the way the provision is created by the assessee. Eventually, after considering the explanation of the assessee, AO disallowed the entire claim of the assessee. AO did not allow even the actual expenditure of Rs.17,37,265/- in the assessment.

Relevant para/lines are extracted as follows :

"6.
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Thus, on the above reasoning I am satisfied that in the present case, estimation for provision is not scientific and sensible and the liability created by way of provision becomes a contingent liability and the same is not allowable under the Income Tax Act. In view of that an amount of Rs.1,05,40,638/- is disallowed and added back to the total income of the assessee. "

6. During the First Appellate proceedings on this issue, assessee made elaborate submissions vide his letter dated 09-12-2015 and submitted that similar issue was subject matter of adjudication before the First Appellate Authority for the A.Y. 2008-09 and the CIT(A) in that case allowed the claim of the assessee relating to the provision of warranty. In effect, the CIT(A) approved the method of arriving the provision created by the assessee. There was detailed discussion by the CIT(A) in the impugned order about the scientific method of accounting the provision of warranty. He also discussed the facts relating to the write back of the excess provision for the taxation in the subsequent year and commented about the absence of any escapement of income on this account of provision of warranty. As per the detailed discussion given in Para No.3.6 of the order of CIT(A), the relief was granted and the provision for warranty was found allowable by the CIT(A). Aggrieved with the same, the Revenue is in appeal with the above grounds. It is the case of the Revenue that CIT(A) erred in allowing the entire claim of

Rs.1,05,40,638/-. Alternatively, CIT(A) erred in not restricting to the actual expenditure of Rs.17,37,265/-.

7. Ld. DR for the Revenue relied heavily on the orders of the AO/CIT(A). However, he has nothing to comment on the finding of the CIT(A) on the same issue in the A.Y. 2008-09.

8. Per Contra, before us on this issue, Ld. Counsel for the assessee brought our attention to the above-mentioned facts. He also relied on the Revenue's divergent stand on this issue in different years. He brought our attention to the fact relating to the relief granted by the CIT(A) in the A.Y. 2008-09 on this issue which became final now. During the second appeal on this issue for the said assessment year, it is a fact that Pune Bench of the Tribunal dismissed the appeal filed by the Revenue on technical ground vide ITA No.339/PN/2015 order dated 30-12-2015. However, the fact is that the issue of provision for warranty for that year has become final and allowable as claimed u/s.37 of the Act. Ld. Counsel for the assessee read out the contents of Para No.3.6 of the order of CIT(A) for the A.Y. 2008-09 where the provision created is Rs.18,68,049/- and utilised Rs.18,01,403/-. The same is found relevant for extraction and the same is reproduced here as under :

*"3.6 Based on the tests laid down by the Hon'ble Supreme Court (in case of Rotork Controls India Pvt. Ltd.) as discussed in Para 3.4 supra, the facts of the present case vis-a-vis the above figures were analyzed. It has been submitted that the provision created during the year is based on **0.4 % of the sale price of equipment**) based on the experience on the Tranter Group since this is only the second year of commercial operations. The appellant has also utilized Rs.18,01,403/- during the impugned year in order to provide the repairs and replacement to its customers. This amount has been credited to the profit & loss account.
.The appellant has also consistently in the current year as well as subsequent FY reversed the amount utilized to the provision for warranty's account, as the aforesaid table would show. On the other hand, the ratio adopted by the A.O. to arrive at the finding that the provisioning has been made on an arbitrary and non-scientific basis does not appear to be very appropriate as is seen have been completed on the total sales, whereas the appellant does not provide warranty on sales made to group companies. The comparison by the assessing officer is also inappropriate as the ratio have been arrived **on the basis of total outstanding warranty liability at the end of the***

year instead of the warranty provided during the year. Accordingly, based on the aforesaid discussion, it would be said that the warranty provisioning by the appellant has been made on scientific and reasonable basis and would represent liability in praesenti and not contingent liability and is therefore allowable deduction u/s.37 of the Income Tax Act. Ground No.1 stands allowed."

9. Further, Ld. Counsel for the assessee brought our attention to the details of the provision of warranty created and utilised over the years since the A.Y. 2007-08 onwards till the A.Y. 2013-14. The data is available in Para 6 of the assessment order. For the sake of completeness, we extract the relevant data here as under :

Particular	FY 2012-13	FY 2011-12	FY 2010-11	FY 2009-10	FY 2008-09	FY 2007-08	FY 2006-07
Net sales on which warranty is provided	828,218,504	874,449,544	862,073,067	705,622,938	627,253,865	459,763,396	272,291,856
Actual warranty utilised during the year towards customer claims	8,365,657	13,129,972	4,137,073	1,737,265	836,093	1,801,403	--
Warranty provision made during the year	13,386,605	3,855,948	8,063,724	10,540,538	836,093	1,868,049	2,397,676

Explaining the above data, Ld. Counsel submitted that the assessee did not utilise any of the provision created in the assessment year 2007-08. Further, the provision created and the utilised amount are more or less the same for the A.Ys. 2008-09 and 2009-10. Referring to the data available relevant for the A.Y. 2012-13, Ld. Counsel submitted that the provision created is only Rs.38,55,948/- against the utilised amount of Rs.1.31 crores. Bringing our attention to the current years data, assessee had to create a provision of Rs.1,05,40,638/- against the utilised amount of Rs.17,37,268/-. Ld. Counsel for the assessee submitted that the excess provision made was credited to the profit and loss account in the subsequent assessment year thereby no loss of revenue is caused by the assessee. Further, he mentioned that creation of provision of warranty in any assessment year constitutes a business decision of the assessee which need not be disturbed by the Revenue so long as the estimation has a reliable basis and the excess provision is offered to tax in the subsequent assessment year. Bringing our attention to the above data, Ld.

Counsel submitted that the assessee has been consistently following the principle of estimation based on 0.4% of the sales price of the equipment based on the experience of the Tranter group. He also mentioned that the warranty becomes payable although the sales pertain to the earlier assessment years. Thus, he pleaded for confirming the order of CIT(A).

10. We have heard both the parties and perused the orders of the Revenue as well as the data placed before us for a decision in the light of the Apex Court judgment in the case of Rotork Controls India Pvt. Ltd. Vs. CIT 314 ITR 62. On perusal of the said judgment, we find the Apex Court explained the conditions relating to the allowability of the expenses of provision for warranty. Relevant lines from the Held portion is extracted as under :

"HELD.
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The present value of a contingent liability, like the warranty expense, if properly ascertained and discounted on accrual basis can be an item of deduction under section 37. The principle of estimation of the contingent liability is not the normal rule. It would depend on the nature of the business, the nature of sales, the nature of the product manufactured and sold and the scientific method of accounting adopted by the assessee. It would also depend upon the historical trend and upon the number of articles produced.

A provision is a liability which can be measured only by using a substantial degree of estimation. A provision is recognized when : (a) an enterprise has a present obligation as a result of a past event; (b) it is probable that an outflow of resources will be required to settle the obligation, and (c) a reliable estimate can be made of the amount of the obligation. If these conditions are not met, no provision can be recognized."

11. From the above facts as well as the legal proposition, it is evident that the provision can be allowed as a allowable deduction subject to the conditions. It is a decided issue, in principle, the provision for warranty is an allowable expenditure subject to the reliable estimations linked to the assessee's obligation to discharge the warranties guaranteed by the assessee at the time of the product sales. In principle, the reliable estimation is also a matter of estimations. Such estimation

may be more in a year or less in other year. In the present case, the assessee estimated the provision at Rs.1,05,40,638/- and the basis of the said estimation is not found erroneous by the AO. The case of the Revenue is that the claim is not allowable as the same is only a provision of warranty. Infact, the Revenue did not even allow the actual expenditure of Rs.17,37,265/- surprisingly. Revenue raised an alternative ground on this part of the decision of the CIT(A). From this point of view, when there is no error noted by the AO in the consistency principle of estimation of 0.4% of the sales price adopted by the assessee together with the fact that the assessee writes back the excess provision as income of the assessee in the subsequent years, we find no reason to allow the grounds raised by the Revenue. Therefore, we are of the view that the decision of CIT(A) is fair and reasonable and it does not call for any interference. Consequently, the Ground No.1 raised by the Revenue is dismissed. Ground No.2 being an alternative Ground is dismissed as academic.

12. In the result, appeal of the Revenue is dismissed.

ITA No.478/PUN/2016 – (By Assessee)

13. Assessee filed this appeal on the solitary issue relating to the write off of the bad debts amounting to Rs.10,08,993/-.

14. Ground raised by the Assessee reads as under :

"1. *Disallowance of bad debts :*

The Ld.CIT(A) erred in confirming the disallowance of an amount of Rs.10,08,993/- in respect of amounts written off by the Appellant as Bad debts, on the ground that the Appellant has failed to establish that during the year the debts in question have become bad. The Appellant prays that the aforesaid disallowance of Rs.10,08,993/- should be deleted and such amount should be allowed as a deduction in computing the total income of the Appellant."

15. Relevant facts and background of this issue include that the assessee claimed Rs.20,29,627/- in the return of income. On scrutiny of the accounts u/s.143(3) of the Act, AO noticed that five of the Debtors namely, Gujarat State Electricity Board, Controller of Stores, Dy. Chief Material Manager, South Central Railways, Fertilisers and Chemicals Travancore Ltd., constitute Governmental bodies/Public Sector undertakings. The total debts receivable by the assessee from these Government bodies works out to Rs.10,08,993/-. Relying on the judgment of Hon'ble Madras High Court in the case of South India Surgical Company Ltd. Vs. ACIT 287 ITR 62, which is relevant for the proposition that the Government cannot be a bad debtor, the AO distinguished the Supreme Court judgment in the case of TRF Ltd. Vs. CIT 190 taxmann 391 (SC) and proceeded to make disallowance by giving the following finding (Para No. 7 of the AO) :

"The Hon'ble Supreme Court held in the above case that it is enough if the Bad Debts is written off as irrecoverable in the accounts of the assessee. The decision of the Hon'ble Supreme Court supports the view that it is only the bad debts which can be as irrecoverable in the books of accounts and not only debts. The decision of the Hon'ble Supreme Court fortifies the stand of the revenue that it is only bad debts that can be written off even after the amendment to section 36(1)(vii).

In view of that an amount of Rs.1,00,89,936/- added back to the total income of the assessee. Penalty proceedings u/s.271(1)(c) are initiated separately for concealment and furnishing inaccurate particulars of income."

16. During the First Appellate proceedings, the assessee furnished written submissions and relied heavily on the Apex Court judgment in the case of TRF Ltd. (supra). It is relevant for the legal proposition *that it is not necessary for the assessee to establish the debt infact has become irrecoverable and it is enough that the bad debt is written off as irrecoverable in the books of account of the assessee.* Thus, the assessee demonstrated before the CIT(A) about the facts relating to the write off in the books of account of the assessee as irrecoverable. Regarding the judgment of Madras High Court in the case of South India Surgical Company Ltd.

(supra), assessee submitted the same is distinguishable on facts. Further, assessee submitted that the order of Mumbai Bench of the Tribunal in the case of Hindustan Thompson Associates Pvt. Ltd. Vs. CIT (2012) 25 taxmann.com 243 is relevant and favourable to the facts of the present case. In the said case, the Tribunal rejected the contention of the Revenue and held that the write off of the short payments as irrecoverable from the customers against the bills raised based on the commercial consideration, constitutes an allowable deduction. The CIT(A) considered the above submissions of the assessee and the case laws and confirmed the addition made by the AO. However, there is no dispute on the fact that the debts in question relate to the short payments on the sale price raised on the debtors and not the entire sale value. He also did not consider the fact that the balance amounts were never to be paid to the assessee as they relate to the reductions in sale price due to delay in supply of material, the quality thereof etc. He also did not mention about how the decision of the Mumbai Bench of the Tribunal in the case of Hindustan Thompson Associates Pvt. Ltd. Vs. CIT (supra) is inapplicable in facts of the present case.

17. Aggrieved with the said decision of CIT(A), assessee filed the present appeal with the grounds extracted above.

18. Before us, Ld. Counsel brought our attention to the ground and submitted that the decision of the CIT(A) is not legally sustainable. The CIT(A) held erroneously that the assessee needs to establish that the debt in question has become bad. There is no dispute about the fact of write off of the said debt as irrecoverable in the books of account of the assessee. Mentioning the facts, Ld. Counsel for the assessee submitted that the debt amounts in question, i.e. Rs.5,10,946/-, Rs.55,473/-, Rs.3,67,846/-, Rs.12,848/-, Rs.61,880/- (Para 7 of the AO's order) and they reflect the balance of amounts receivable from the

Governmental bodies and the same are relatable to the reductions made by the debtors due to bad delivery/delay in delivery of the goods to the Government bodies. From this point of view, it is the argument of Ld. Counsel for the assessee, strictly speaking, these are not bad debts. They are a kind of discounts demanded by the debtors out of the sale price for not complying with the delivery schedules. Since the assessee has already complied with the legal requirement of writing off in the books of the accounts as irrecoverable, it is good enough for applying the ratio laid down by the Hon'ble Apex Court in the case of TRF Ltd. (supra). Thus, the Ld. Counsel prayed for reversing the order of the AO/CIT(A) on this issue and allow the ground raised by the assessee.

19. In reply, Ld. DR for the Revenue relied heavily on the orders of the AO and the CIT(A) dutifully. He also relied on the judgment of Hon'ble Madras High Court in the case of South India Surgical Company Ltd. (supra). However, he has not controverted the facts relating to the nature of debts which are basically discounts or reduced/adjusted sale price due to delay in deliveries of the material by the assessee to the said Governmental bodies/Public Sector undertakings.

20. We have heard both the parties on this issue relating to 'bad debts' and perused the orders of the Revenue as well as the Paper book filed before us. There is no dispute on the facts that the parties involved are the Governmental bodies (Ministry of Railways/State Electricity Board/Public Sector undertakings). Further, we find that the debts in question directly related to the reduced sales price. It is also an undisputed fact that the balance amounts receivable by the assessee are never to be received as they relate to the discounted sales price owing to delay in delivery of the material to the said Governmental bodies. Further, we also noticed that assessee has actually written off these debt amounts as irrecoverable in the books of account of the assessee. Considering all these facts, in our opinion, these

facts are not comparable to the facts discussed in the judgment of Hon'ble Madras High Court in the case of South India Surgical Company Ltd. (supra). Consequently, the ratio of the Hon'ble Apex Court judgment in the case of TRF Ltd. (supra) becomes applicable to the facts of the present case. From this point of view, we are of the opinion that the order of CIT(A)/AO are required to be reversed. Accordingly, the solitary ground raised by the assessee is allowed.

21. In the result, appeal of the Assessee is allowed.

22. To sum up, appeal of the Revenue is dismissed and the appeal of the Assessee is allowed.

Order pronounced on this 09th day of February, 2018.

Sd/-
(SUSHMA CHOWLA)
न्यायिक सदस्य / JUDICIAL MEMBER

Sd/-
(D.KARUNAKARA RAO)
लेखा सदस्य / ACCOUNTANT MEMBER

पुणे / Pune; दिनांक Dated : 09th February, 2018.
Satish

आदेश की प्रतिलिपि अग्रेषित/Copy of the Order is forwarded to :

1. अपीलार्थी / The Appellant;
2. प्रत्यर्थी / The Respondent;
3. आयकर आयुक्त(अपील) / The CIT(A)-5, Pune
4. आयकर आयुक्त / The CIT-5, Pune
5. विभागीय प्रतिनिधि, आयकर अपीलीय अधिकरण, पुणे "बी" / DR 'B', ITAT, Pune;
6. गार्ड फाईल / Guard file.

आदेशानुसार/ BY ORDER,

सत्यापित प्रति //True Copy//

Senior Private Secretary
आयकर अपीलीय अधिकरण ,पुणे / ITAT, Pune