IN THE INCOME TAX APPELLATE TRIBUNAL
"E" Bench, Mumbai

Before Shri G. Manjunatha, Accountant Member
and Shri Ravish Sood, Judicial Member

ITA No.1175/Mum/2016
(Assessment Year: 2010-11)

Shamas Tabrez Gulam Madni Ansari, C/o,D.C. Bothra & Co. (CA)297, Tardeo Road, 1st Floor Willie Mansion, Opp. Bank of India, Chowk, Mumbai – 400 007	Vs.	I.T.O. 18(1)(2)(erstwhile) ACIT 21(3) (Present),1st Floor, Piramal Chamber,Lala Baug, Mumbai - 400012

PAN – ADZPA5475H

(Appellant) **(Respondent)**

Appellant by: Shri Pavan Ved, A.R
Respondent by: Shri Amit Pratap Singh, D.R

Date of Hearing : 10.10.2019
Date of Pronouncement: 18.10.2019

O R D E R

PER RAVISH SOOD, JM

The present appeal filed by the assessee is directed against the order passed by the CIT(A)-33, Mumbai, dated 11.12.2015, which in turn arises from the order passed by the A.O under Sec. 143(3) of the Income Tax Act, 1961 (for short 'Act'), dated 28.03.2013 for A.Y. 2010-11. Assessee has assailed the impugned order on the following grounds of appeal before us:

"1. That on facts and circumstances of the case and in law the ld. C.I.T.(Appeals) has erred in confirming the addition made u/s. 41(1) by ld. Assessing Officer at Rs.2,83,39,538/- and at Rs.1,53,96,597/- respectively without properly appreciating the facts of the case and legal position. As the total addition made u/s.41(1) at Rs.4,37,36,135/- by the ld. A.O. and confirmed by ld. C.I.T.(Appeals) is wrong on facts and bad in law, therefore appellant prays that same may kindly be deleted.

2. That the ld. C.I.T.(Appeals) has erred in law as well as on facts in confirming the disallowance made by the ld. A.O. u/s. 40A(3) at Rs.4,84,160/- without properly appreciating the facts of the case. As the disallowance made u/s. 40A(3) at Rs.4,84,160/- by the ld.

A.O. and confirmed by Id. C.I.T.(Appeals) is wrong on facts and bad in law, therefore appellant prays that same may kindly be deleted.

3. That the appellant craves the leave to amend, alter, substitute and or to raise new or additional grounds of appeal at the time of hearing."

2. Briefly stated, the assessee who is engaged in the business of manufacturing and export of ladies embroidery garments had filed his return of income for A.Y. 2010-11 on 15.10.2010, declaring his total income at Rs.14,37,120/-. The return of income filed by the assessee was processed as such under Sec. 143(1) of the Act. Subsequently, the case of the assessee was selected for scrutiny assessment under Sec.143(2).

3. During the course of the assessment proceedings the A.O in order to verify the genuineness of the "Sundry creditors" appearing in the 'balance sheet' of the assessee for the year under consideration, issued notices under Sec. 133(6) to some of the parties, as under :

Sr. No.	Name of the party	Amount standing
1.	M/s. S.S Handloom	Rs. 25,00,000/-
2.	M/s Nidhi Textiles	Rs. 27,88,159/-
3.	Kenzab Garments	Rs. 27,98,457/-
4.	Fab Fashion	Rs. 25,42,670/-
5.	Iram Fashion Wear	Rs. 28,52,710/-
6.	Haji Sood & Co.	Rs. 32,49,180/-
7.	New Fashion Garments	Rs. 31,00,000/-
8.	Adi Fabrics	Rs. 27,92,810/-
9.	Zeenat Art Fashion	Rs. 27,69,440/-
10.	Unaid	Rs. 29,46,112/-
	Total	Rs.2,83,39,538/-

All the aforesaid notices were returned by the postal authorities with the remarks 'left' or 'not known'. In the backdrop of the aforesaid facts, the A.O directed the assessee to produce the aforementioned parties along with the supporting documentary evidence. Although, the assessee promised to produce the aforementioned parties, however, he failed to comply with the directions of the A.O. Also, no confirmations of the aforesaid parties were filed by the assessee in the course of the assessment proceedings. Observing, that there was absolute no movement in the balances appearing in the respective accounts of the aforesaid 10 parties for the last 3 years, the A.O added the aggregate amount of Rs.2,83,39,538/- as the income of the assessee under Sec.41(1) of the Act. Apart there from, it was observed by the A.O, that there was also no movement in the accounts of the following 11 "Sundry creditors" for the last 3 years:

Sr. No.	Name of the party	A.Y. 2008-09	A.Y. 2009-10	A.Y. 2010-11
1.	Keni Garments	20,96,715	20,96,715	20,96,715

2.	Munnaf & Co.	20,53,480	20,53,480	20,53,480
3.	Natraj Sales	24,68,112	24,68,112	24,68,112
4.	Nidhi Plus	35,42,810	35,42,810	35,42,810
5.	Bhagalpur Handloom Fabricks	7,36,475	7,36,475	7,36,475
6.	Sambhav Garments	14,75,080	14,75,080	14,75,080
7.	S.B. Handloom Fabrics	5,65,643	5,65,643	5,65,643
8.	Technomax	5,39,360	5,39,360	5,39,360
9.	Neelkamal Fabrics	6,36,492	6,36,492	6,36,492
10.	M.M. Gandhi	5,90,368	5,90,368	5,90,368
11.	M. Gandhi	6,91,342	6,91,342	6,91,342
	Total			1,53,96,597

The A.O directed the assessee to file the confirmations of the aforesaid 11 parties. As the assessee failed to comply with the directions of the A.O, therefore, he treated the aforesaid amount of Rs.1,53,96,597/- also as the income of the assessee under Sec. 41(1) of the Act. Further, the A.O while framing the assessment observed, that the assessee during the year had made cash payments towards 'labour charges' aggregating to Rs.4,84,160/- to M/s Sadiya Art. As the payments made to the aforesaid concern on all the 12 occasions were found to be in excess of an amount of Rs.20,000/-, therefore, the same were disallowed by the A.O under Sec.40A(3) of the Act. On the basis of his aforesaid deliberations the A.O assessed the income of the assessee at Rs.4,56,57,420/-.

4. Aggrieved, the assessee assailed the assessment framed by the A.O before the CIT(A). Observing, that the assessee had failed to prove that the outstanding liabilities towards the aforesaid 21 parties aggregating an amount of Rs.4,37,36,135/- did still persist, therefore, the CIT(A) finding no infirmity in the view taken by the A.O upheld the addition that was made by him under Sec. 41(1) of the Act. Insofar the disallowance under Sec. 40A(3) of the 'labour charges' that were paid by the assessee to M/s Sadiya Art was concerned, the same too was confirmed by the CIT(A).

5. The assessee being aggrieved with the order passed by the CIT(A) has carried the matter in appeal before us. The ld. Authorized Representative (for short 'A.R') for the assessee, took us through the facts of the case. It was vehemently submitted by the ld. A.R, that as the liabilities towards the aforesaid 'Sundry creditors' were acknowledged by the assessee as outstanding in his 'books of accounts', therefore, the lower authorities were in error in characterising the same as ceased liabilities under Sec.41(1) of the Act. It was further submitted by the ld. A.R, that insofar the outstanding liability of Rs. 2,83,73,983/- that was due

by the assessee towards the aforesaid 10 parties was concerned, the same were partly paid off by the assessee during the succeeding years and the aggregate of the balance outstanding liability was reduced to an amount of Rs.1,02,11,715/- in the year 2017. In the backdrop of the aforesaid facts, it was averred by the ld. A.R, that now when the assessee had discharged part of its outstanding liability towards the aforesaid parties, therefore, it was incorrect on the part of the lower authorities to have characterised the said creditors as a ceased liability. As regards the balance outstanding liability of Rs.1,02,11,715/- pertaining to the aforesaid 10 parties, and also the liability towards the remaining 11 creditors aggregating to Rs.1,53,96,597/-, it was averred by the ld. A.R, that as the same had not been "written off" by the assessee in its 'books of accounts' and was acknowledged as its outstanding liabilities, therefore, the lower authorities were not justified in holding the same as a ceased liability under Sec.41(1) of the Act. In support of his claim that where in the subsequent years the creditors had been paid off by an assessee, the same can by no stretch of imagination be held as a ceased liability within the meaning of Sec.41(1), the ld. A.R relied on the judgment of the **Hon'ble High Court of Bombay** in the case of **PCIT-19, Vs. Pukhraj S. Jain (ITA No. 1288 of 2016, dated 04.01.2019)**. Also, in order to drive home his claim, that an outstanding liability cannot be held to have ceased under Sec.41(1), merely for the reason that the same is outstanding in the 'books of accounts' of assessee for a number of years, the ld. A.R had drawn support from the judgment of the **Hon'ble High Court of Bombay** in the case of **PCIT-1 Vs. Mahalaxmi Infra Projects Ltd. (ITA No.1769 of 2016, dated 30.01.2019).** It was submitted by the ld. A.R, that as the sundry creditors were reflected as outstanding liabilities in the 'books of accounts' of the assessee, the same thus could not have been held to have ceased under Sec.41(1). Ld. A.R drawing support from the order of the **ITAT Delhi Bench "G"** in the case of **Satpal & Sons (HUF) Vs. ACIT Circle-38(1), New Delhi (2017) 166 ITD 616 (Del)** submitted, that even in case the creditors were not found available at the addresses provided and their PAN were also not found to be valid, no addition could be validly made u/s 41(1) on the said standalone basis. Further, the ld. A.R had relied on the order of **ITAT 'A' Bench, Mumbai** in the case of **ACIT-17(1), Mumbai Vs. Kokan Mercantile Co-operative Bank Ltd. (ITA No. 766/Mum/2014, dated 07.03.2018)**. On the basis of his aforesaid contentions, it was averred by the ld. A.R that the lower authorities were in error in treating the outstanding liabilities of Rs.4,37,36,135/- due by the assessee towards its sundry creditors as a ceased liability under Sec.41(1) of the Act. As

regards the disallowance of Rs.4,84,160/- that was made by the A.O under Sec. 40A(3), it was submitted by the ld. A.R, that no proper opportunity was given by the A.O while making the said disallowance. Accordingly, it was submitted by the ld. A.R, that in all fairness the matter may be restored to the file of the A.O for fresh adjudication after affording sufficient opportunity of being heard to the assessee.

6. Per contra, the ld. Departmental Representative (for short 'D.R') submitted, that the notices issued under Sec.133(6) by the A.O to the 10 sundry creditors aggregating to Rs.2,83,39,538/- were returned back by the postal authorities with the remarks 'left' or 'not known'. It was the claim of the ld. D.R, that the A.O after making proper and independent inquiries had rightly concluded that the liabilities aggregating to Rs.4,37,36,135/- had ceased within the meaning of Sec.41(1) of the Act. Apart there from, it was submitted by the ld. D.R, that as regards the liability of Rs.1,53,96,597/- shown by the assessee against the remaining 11 parties, it was an admitted fact on the part of the assessee that no payment was made to either of the said parties till date. Adverting to the disallowance made by the A.O under Sec. 40A(3), it was the claim of the ld. D.R, that as the case of the assessee did not fall within the purview of any of the exception carved out in Rule 6DD of the Income Tax Rules, 1962, therefore, the A.O had rightly disallowed the same.

7. We have heard the authorized representatives for both the parties, perused the orders of the lower authorities and the material available on record, as well as the judicial pronouncements relied upon by them. As is discernible from a perusal of Sec.41(1) of the Act, in case an allowance or deduction has been made in the assessment for any year in respect of loss, expenditure or trading liability incurred by the assessee, and subsequently during any previous year, the assessee has obtained, whether in cash or in any other manner whatsoever, any amount in respect of such loss or expenditure or some benefit in respect of such trading liability by way of remission or cessation thereof, the amount obtained by the assessee or the value of benefit accruing to him shall be deemed to be profits and gains of business or profession and accordingly chargeable to income tax as the income of that previous year. Admittedly, the assessee had claimed deduction of the amounts aggregating to Rs. 4,37,36,135/- reflected against the aforesaid 21 sundry creditors. The liabilities towards the said

"Sundry creditors" is acknowledged by the assessee in its 'books of account' for the year under consideration. In other words, the assessee had not "written off" the outstanding liabilities towards the aforesaid sundry creditors in its accounts. As can be gathered from the orders of the lower authorities, the liabilities shown by the assessee against the aforesaid sundry creditors has been held by them to have ceased to exist within the meaning of Sec.41(1) of the Act, for the reason, that the same were outstanding since long and there was no movement in their respective accounts. In sum and substance, as the assessee had not discharged the aforesaid outstanding liabilities, therefore, the said reason had primarily weighed in the mind of the A.O for treating them as a ceased liability. Apart there from, we find, that as the notices issued under Sec.133(6) to the aforesaid parties were returned unserved and the assessee also could not furnish the confirmations of the parties acknowledging the amount due from the assessee, therefore, the A.O held a conviction that as the said parties were non-existent, therefore, it could safely be concluded that the liability of the assessee towards them had ceased to exist.

8. We have given a thoughtful consideration to the facts of the case in the backdrop of the contentions advanced by the authorized representatives for both the parties. In our considered view, the mere fact that a liability towards a party is outstanding in the 'books of account' of an assessee since long, cannot *ipso facto* justify characterising of the same as a ceased liability. In fact, we are of a strong conviction, that for invoking the provisions of Sec. 41(1), it has to be shown that the assessee had obtained, some benefit in respect of the trading liability under consideration by way of remission or cessation thereof during the year under consideration. In sum and substance, for invoking the provisions of Sec. 41(1), it has to be irrefutably shown that some benefit in respect of the 'trading liability' had been obtained by the assessee by way of remission or cessation of the same. In the case before us, we find, that the assessee had duly acknowledged his liability towards the sundry creditors in his books of accounts. Accordingly, merely for the reason that the liability towards the aforesaid 21 sundry creditors was outstanding in the accounts of the assessee for the last many years, in our considered view would not suffice for bringing the same within the realm of the provisions of Sec.41(1) of the Act. Our aforesaid view is fortified by the judgment of the **Hon'ble High Court of Bombay** in the case of **PCIT-1 Vs. M/s Mahalaxmi Infra Projects Ltd. (ITA No. 1769 of 2016, dated**

30.01.2019). In the aforesaid case, it was observed by the Hon'ble High Court that merely because a period of 3 years had expired from arising of the liability would not automatically mean that the liability has ceased. Also, a similar view had been taken by the **Hon'ble High Court of Delhi** in the case of **CIT Vs. Jain Exports Pvt. Ltd. (2013) 85 CCH 66 (Del)**. In the said case, it was observed that in order to attract the provisions of Sec. 41(1), it was necessary that there should have been a cessation or remission of liability. Relying on the judgment in the case of J.K Chemicals Ltd. Vs. CIT (1966) 62 ITR 34 (Bom), the Hon'ble High Court had observed that cessation of liability may occur either by the reason of the liability becoming unenforceable in law by the creditor where the debtor had declared his intention not to honour the liability, or there was a contract between parties or by discharge of the debt. Also, it was observed by the Hon'ble High Court that the fact that enforcement of a debt was barred by limitation would not *ipso facto* lead to the conclusion that there was a cessation or remission of liability.

9. In the case before us, the outstanding liabilities of the assessee can be compartmentalised into two parts viz. (i) outstanding liabilities which had moved/partly discharged in the subsequent years; and (ii) the liabilities which had remained unmoved and were outstanding as such in the accounts of the assessee. As far as the liabilities of Rs.1,81,62,268/- [Rs.2,82,72,983/- (-) Rs.1,02,11,715/-], we are of the considered view, that as the same had been discharged by the assessee in the subsequent years, therefore, the same could by no stretch of imagination could be held to have ceased during the year. Our aforesaid view is fortified by the judgment of the **Hon'ble High Court of Bombay** in the case of **PCIT-19, Vs. Pukhraj S. Jain (ITA No. 1288 of 2016, dated 04.01.2019)** and that of the Hon'ble High Court of Punjab & Haryana in the case of **CIT Vs. Speedways Tyre Ltd. (2014) 364 ITR 401 (P&H).** Insofar, the remaining outstanding liabilities of Rs.1,02,11,715/-, and Rs.1,53,96,597/- (11 parties) are concerned, we are of the considered view, that as the assessee had acknowledged his liability towards the said parties, therefore, the same merely for the reason that the said liabilities are outstanding for the last many years in the 'books of accounts' of the assessee cannot justify bringing the same within the realm of the provisions of Sec.41(1) of the Act. Apart there from, we may also observe, that there is nothing discernible from the orders of the lower authorities which would justify relating the impugned cessation of the outstanding

liabilities to the year under consideration viz. A.Y. 2010-11. As observed by us hereinabove, before an outstanding liability is to be characterised as a ceased liability, it has to be shown, that the assessee had obtained some benefit in respect of such trading liability during the said previous year. In sum and substance, it is not permissible for the revenue to treat a ceased liability as the income of the assessee in any year of its choice. As per mandate of law, it is obligatory on the part of the revenue to show that the assessee had obtained some benefit in respect of such trading liability during the year, before the same is deemed as its profits and gains of business or profession for the said year. On the basis of our aforesaid deliberations, we are of the considered view, that it can safely be concluded that as the assessee had acknowledged his outstanding liabilities towards the aforesaid parties in its 'books of accounts', therefore, merely for the reason that the same is outstanding for the last many years would not suffice for characterising of the same as a ceased liability in his hands. Apart there from, we are also unable to comprehend as to on what basis the aforesaid impugned cessation of liability had been related by the A.O to the year under consideration i.e A.Y. 2010-11. On the basis of our aforesaid observations, we are of the considered view, that as the requisite conditions for invoking the provisions of Sec.41(1) are not found to have been satisfied in the case before us, therefore, we have no hesitation in concluding that the addition of Rs.4,37,36,135/- made by the AO under Sec.41(1) of the Act cannot be sustained and is liable to be vacated. Accordingly, the aforesaid addition of Rs.4,37,36,135/- sustained by the CIT(A) is deleted.

10. We shall now advert to the disallowance of Rs. 4,84,160/- made by the A.O under Sec. 40A(3) of the Act. As observed by us hereinabove, the assessee had made a payment aggregating to Rs.4,84,160/- towards 'labour charges'' to M/s Sadiya Art. On all of the 12 occasions, the respective payments made by the assessee to the aforesaid concern were found to be in excess of Rs.20,000/-. We have given a thoughtful consideration and are unable to persuade ourselves to subscribe to the claim of the assessee that no sufficient opportunity was provided to him by the lower authorities in context of the aforesaid disallowance. In fact, we find, that the assessee had assailed the aforesaid disallowance made by the A.O u/s 40A(3), on the ground, that the genuineness of the labour charges paid by the assessee to M/s Sadiya Art was not in dispute. In our considered view, as admittedly the payments made by the assessee to M/s Sadiya Art, on all the occasions had exceeded an amount of Rs. 20,000/-, therefore, the

A.O had rightly disallowed the said payments aggregating to Rs. 4,84,160/- under Sec. 40A(3). Apart there from, we find that it is not the case of the assessee that the incurring of the aforesaid cash expenditure was covered by any of the exceptions carved out in Rule 6DD of the Income Tax Rules, 1962. In the backdrop of the aforesaid facts, we find no infirmity in the order of the CIT(A), who in our considered view had rightly concluded that the 'labour charges' of Rs.4,84,160/- paid by the assessee in cash to M/s Sadiya Art in excess of the prescribed limits were clearly hit by the provisions of Sec. 40A(3) of the Act. Accordingly, the disallowance of Rs.4,84,160/- made by the A.O under Sec. 40A(3) of the Act is upheld. The **Ground of appeal No. 2** is dismissed.

11. The appeal of the assessee is partly allowed in terms of our aforesaid observations.

Order pronounced in the open court on 18.10.2019

Sd/-	Sd/-
(G.Manjunatha)	(Ravish Sood)
ACCOUNTANT MEMBER	JUDICIAL MEMBER

मुंबई Mumbai; दिनांक. 18.10.2019
PS. Rohit

आदेशकीप्रतिलिपिअग्रेषित/Copy of the Order forwarded to :

1. अपीलार्थी/ The Appellant
2. प्रत्यर्थी/ The Respondent.
3. आयकरआयुक्त(अपील) / The CIT(A)-
4. आयकरआयुक्त/ CIT
5. विभागीयप्रतिनिधि, आयकरअपीलीयअधिकरण, मुंबई/ DR, ITAT, Mumbai
6. गार्डफाईल / Guard file.

सत्यापितप्रति //True Copy//

आदेशानुसार/ BY ORDER,

उप/सहायकपंजीकार (Dy./Asstt. Registrar)

आयकरअपीलीयअधिकरण, मुंबई / **ITAT, Mumbai**