



IN THE INCOME TAX APPELLATE TRIBUNAL

"C" BENCH, MUMBAI

BEFORE SHRI MAHAVIR SINGH, VICE PRESIDENT AND

SHRI S. RIFAUR RAHMAN, ACCOUNTANT MEMBER

ITA no.2317/Mum./2019
(Assessment Year : 2013-14)

Dy. Commissioner of Income Tax
Large Tax Unit-1, Mumbai

..... Appellant

v/s

M/s. CMI FPE Limited
Plot no.64, Mehta House
Road no.13, MIDC
Andheri (E), Mumbai 400 093
PAN – AAACF0252G

..... Respondent

Revenue by : Shri Shreekala Pardesi
Assessee by : Shri Viraj Mehta

Date of Hearing – 25.03.2021

Date of Order – 02.06.2021

ORDER

PER S. RIFAUR RAHMAN, A.M.

The Revenue is in appeal against the order of Commissioner of Income Tax (Appeals)-3, Mumbai, dated 5.11.2018, by raising following grounds of appeal:-

- 1. Whether On the facts and in the circumstances of teh case and in law, the learned CIT(A) was right in deleting the disallowance of the provision for loss on contracts amounting to ₹ 3,46,82,672, made by the Assessing Officer.*
- 2. Whether On the facts and in the circumstances of the case and in law, the learned CIT(A) was right in allowing the provision for doubtful debts claimed by the assessee in computation of*

book profit under section 115JB of the Act, especially in view of the fact that the decision of the Hon'ble Supreme Court in the case of Vijaya Bank v/s CIT, [2010] 323 ITR 166 (SC) is applicable only to Banking Companies.

2. At the time of hearing, it was brought to our notice that ground No. 1 and 2 are covered by the order of coordinate bench in the case of assessee in earlier assessment years. Ld DR agreed with the above submissions. Therefore, we proceed to dispose off this appeal as such by bringing on the relevant facts on record.

3. With regard to ground No. 1, it is contested that Ld. CIT(A) deleted the disallowance of the provision for loss on contract accounting to the extent of ₹ 3,46,82,672, made by the Assessing Officer. We notice that this issue was already considered by Co-ordinate Bench in assessee's own case in ITA No.2334/Mum./2013 for the assessment year 2009-10. For the sake of clarity, the observation of the Bench it is reproduced below:-

"3. We have heard the parties, and perused the material on record. 3.1 The assessee is a manufacturer of heavy industrial machinery, which has a gestation period of two to three years. It follows accrual system of accounting, which is mandatory for it under its' governing Act, i.e., the Companies Act, 1956. It follows percentage completion method for recognition of revenue. The fundamental accounting principle of prudence, providing for all known liabilities and losses (even though the amount thereof cannot be determined with certainty and represents only a best estimate in the light of available information), would validate the assessee's claim. The said principle, along with 'substance over form' and 'materiality', constitute the principal considerations for the selection of the accounting policies. As such, irrespective of the stage of

completion of the project, where, on the basis of the facts and data, a project stands to incur a loss on its' completion, the same is to be provided in the first instance, and which has been provided for by the assessee on proportionate basis. The said principle stands advocated by both the Accounting Standard (AS-1) issued by ICAI as well as AS-I issued u/s. 145 by CBDT, both since notified, so as to assume the force of law. The same would entail carrying out a cost- benefit analysis, which may itself involve several estimates, called accounting estimates. The same have to be reliable, based on verifiable and/or empirical data, which we regard as a second, albeit integral, aspect - the assessee's claim for loss meriting an in principle approval or acceptance. True, in a given case, the loss itself may arise only on account of inflated cost, so that on facts there is no application of the principle, but that would not detract from the fact that such a loss, where properly made, cannot be denied. Further, the estimate may itself change from time to time, i.e., as time goes by and more and more work, incurring cost, is undertaken, so that it is only the balance (uncompleted) work, i.e., which is yet to be completed, qua which the costs are to be estimated. The cost estimate is again bound to vary on the basis of and in light of the available information. That (variation), rather, is the norm, as inflow of information, having both qualitative and quantitative implications, and ITA No. 2334/Mum/2013 (A.Y. 2009-10) CMI FPE Limited vs. Asst. CIT-LTU which aspects are themselves interrelated, is a continuous phenomenon. To contend, therefore, as does the Id. CIT(A), that there has been a variation, and inferring on that basis that the estimates are not scientific or not based on reliable data, is misconceived. In fact, the variation, as reported (refer para 4 of the impugned order), is itself quite insignificant, so that it should not have, even on that basis, led to the inference of rejection of the estimates.

The Revenue can no doubt, and it is indeed duty bound to, verify the assessee's claim qua both the cost and the revenue estimates. Why, in a given case, the actual costs, incurred subsequently, may itself form a valid ground or basis to verify the veracity of the assessee's claim/s, even as we have clarified that the estimates are bound to undergo change with time in light of the available information and experience, so that the principle involved would be that the estimate or assessment as made is explainable with reference to the available information.

3.2 The Revenue misdirects itself when it, relying on the decision *Rotork Controls India Private Ltd. vs. CIT* [2009] 314 ITR 62 (SC), refers to the statement of law by the Hon'ble Apex Court in respect of claim for deduction qua a liability. The two, i.e., a 'liability' and 'loss', though para materia from the stand-

point of prudence, may not be so as regards provision therefor. The provision of loss would be justified on a factual basis to arrive at the conclusion that the estimated expenditure (for the work to be undertaken or the services to be rendered), together with the actual cost already incurred thereon, shall exceed the estimated revenue from the project. The question, thus, is principally of the reliability of the estimate, given the explicit terms of the accounting standards, statutorily mandated, so that the same have the force of law, with the Apex Court in fact emphasizing time and again that in the absence of any specific provision of law to the contrary, the principles of commercial accounting shall apply. Reference in this regard may also be made with profit to its' celebrated decision in Calcutta Co. Ltd. vs. CIT [1959] 37 ITR 1 (SC). Once, on the basis of the ITA No. 2334/Mum/2013 (A.Y. 2009-10) CMI FPE Limited vs. Asst. CIT-LTU facts and the information on record, the loss is likely to arise, the same has to be provided for under the prudence mandate, which is what AS-7 (also notified by the Central Government) in substance provides under the segment 'Recognition of expected losses' vide paras 35 and 36, reproduced as under:

'Recognition of Expected Losses

35. When it is probable that total contract costs will exceed total contract revenue, the expected loss should be recognised as an expense immediately.

36. The amount of such a loss is determined irrespective of:
a) whether or not work has commenced on the contract;

b) the stage of completion of contract activity; or the amount of profits expected to arise on other contracts which are not treated as a single construction contract in accordance with paragraph 8.' A liability, on the other hand, arises on account of a contractual or statutory obligation.

3.3 As regards the reliance by the Revenue before us on CIT vs. Kamani Metals & Alloys Ltd. [1994] 208 ITR 1017 (Bom), the same, in our view, shall not govern the facts or the issue involved in the present case, even as admittedly the accountancy principle of valuation of inventories is also based on the principle of prudence. In that case, the assessee-company, a manufacturer of copper and copper based alloys, strips and coils of various specifications, valued its raw materials, being virgin metals (viz. copper, zinc, tin), following the valuation principle of cost or replacement value, whichever is less. On that basis, it claimed the reduction in the raw material (copper cathode) price

post December 31, 1974, the valuation date, for which the purchase order was issued in August, 1974. The Hon'ble Court upheld the order by the tribunal, restricting the valuation to that as per the rate obtaining as on 31.12.1974, i.e., in principle. Further, however, as the goods had not been received by December 31, 1974, so that there was no closing stock as on that date, the Hon'ble Court held that ITA No. 2334/Mum/2013 (A.Y. 2009-10) CMI FPE Limited vs. Asst. CIT-LTU the reduction in the price with reference to the contract date even as on 31.12.1974 also could not allowed. Further, even though the value of the raw material cost may have decreased, the firm may stand to earn profit on the basis of the net realizable value of the finished goods, i.e., on the basis of the ruling price less cost of realization thereof. The prices of finalized goods may or may not move in sympathy with that of the raw materials, depending upon the demand and supply forces in the relevant market. Two, even the raw material price may stand to reverse, and may not be irreversible so as to conclude that the loss had indeed been incurred. Thirdly, and most importantly, it is the profit (or loss) for the relevant year that is to be assessed and brought to tax for that year - each year being an independent unit of assessment. The decline in the market price, even where relevant and material, i.e., with reference to the price obtaining as at the year-end, would therefore fall to be considered as and form part of the profit (or loss) of the subsequent year. This also explains the standard prescription for valuing raw material at historical cost (refer AS-2 issued by ICAI). The project/s in the instant case, on the other hand, spread over 2-3 years, and it is on account of this that the loss thereon, the enterprise following percentage completion method (for recognizing income), the profit (or loss) on the entire project, estimating the costs yet to be incurred, is required to be reckoned, booking the same proportionately. AS-7, on the other hand, clearly provide for reporting profit on the basis of proportionality when the project is likely to yield a profit, while booking the loss where not so, and which in the present case, as we understand, has been provided for on a proportionate basis. The reliability of the estimate is indeed very relevant and crucial to the claim for loss, lest any amount could be claimed under the garb of the likely loss, and which brings us to the next aspect of the matter.

3.4 The Revenue, moving on the premise that the assessee's claim is both factually and legally untenable, has rejected the same. We find no exercise conducted by it at any stage to verify the assessee's claim, which we have found acceptable in principle.

ITA No. 2334/Mum/2013 (A.Y. 2009-10) CMI FPE Limited vs. Asst. CIT-LTU In this respect, the Id. AR would before us contend that the assessee has also, and only rightly so, taken into account the likely cost escalations; the projects being scheduled to be completed only over a period of two to three years. True, but the same would also have been similarly factored into while negotiating the contract rates. The matter would require being examined for the veracity of the estimations, and particularly qua cost escalations, as also with reference to the relevant clauses, if any, of the contract, i.e., as regards the cost escalation, which could also be made operative where the project is delayed beyond a particular time line. Reference in this context may also be made to paras 22, 23 and 31 of AS-7.

4. In view of the foregoing, we uphold the assessee's claim in principle, i.e., qua the provision for loss on contracts likely to arise on its ongoing projects, which though would have to be substantiated. Further, the fact that the assessee did not contest the claim for loss, similarly made, while computing its' book profit, though surprising, cannot by itself prevail so as to be regarded as conclusive of the matter, and can at best provide a clue to the Revenue that the assessee's claim with regard to cost escalation/s may require a closer examination, which the AO is even other obliged to, even as to be fair to the assessee the loss stands provided for in the audited accounts, so that it has been subject to both internal as well as external scrutiny. The same though cannot bind the A.O. We decide accordingly. The appeal is accordingly disposed on the above said terms."

4. Respectfully following the above decision of the Co-ordinate Bench, we inclined to dismiss the ground No.1 raised by the Revenue.

5. With regard to ground No.2, it is contested that Ld CIT(A) erred in allowing the provisions for doubtful debts claimed by the assessee in computation of book profit under section 115JB of the Act. We notice that this issue also covered in favour of the assessee by the Co-ordinate Bench decision in assessee's own case in ITA No. 2777/Mum./2016 for assessment year 2010-11 dated 07.03.2018. In turn, the

Co-ordinate Bench allowed the appeal of the assessee by relying on the Co-ordinate Bench decision in the case of ITA No.1073/Mum./2005 in DCIT v/s Trent Ltd., dated 18.5.2012. For the sake of clarity, the observations of the Bench is reproduced below:–

"5. We have heard the argument advanced by the Ld. Representative of the parties and perused the record. The Ld. Representative of the assessee has argued that this issue has already been remanded before the AO while deciding the case by the Mumbai ITAT in ITA. No.2334/M/2013 for the A.Y. 2009-10 by virtue of order dated 10.06.2016, therefore, accordingly, this issue is being liable to be restored before the AO to examine and decide afresh. Copy of order dated 10.06.2016 in ITA. No.2334/M/2013 for the A.Y. 2009-10 in the assessee's own case is on the file in which the issue has already remanded before the AO to decide afresh by giving an opportunity of being heard to the assessee in accordance with law. Since, this issue is pending before the AO for the A.Y. 2009-10, therefore, we set aside the finding of the CIT(A) on this issue and remand this issue before the AO to decide the matter of controversy afresh in view of the direction raised by the Hon'ble ITAT in ITA. No.2334/M/2013 for the A.Y. 2009-10 dated 10.06.2016. Accordingly, this issue is decided in favour of the assessee against the revenue.

ISSUE NO. 2:-

6. Under this issue the assessee has challenged the confirmation of the action of the AO in adding back the provision for doubtful debts ITA Nos. 2777/Mum/2016 2778/Mum/2016 A.Y. 2010-11 & 2011-12 of Rs.15,30,51,618/- while computing book profits u/s 115JB of the Act. The Ld. Representative of the assessee has argued that this issue has already been covered by the Hon'ble ITAT in ITA. No.1073/M/2005 dated 18.05.2012. The copy of order in ITA. No.1073/M/2005 dated 18.05.2012 is on the file, we noticed that the similar type of provision i.e., provision for doubtful debts has already been allowed by the Hon'ble ITAT by relied upon the decision of the Hon'ble Supreme Court in the case of Vijaya Bank Vs. CIT, 323 ITR 166 (SC) and in the case of CIT Vs. Yokogawa India Ltd., (2012) 204 Taxman 305 (Kar.). Before going further, we deemed it necessary to advert the finding of the Tribunal on record: -

"10. On ground no.2, the learned Counsel submitted that the assessee has made a provision for doubtful debt and reduced the said provision from current assets disclosed in the balance sheet. On these facts, it is argued that clause (i) of Explanation (1) of section 115JB of the Act, cannot be applied in view of the judgment of the Hon'ble Supreme Court in *Vijaya Bank v/s CIT*, 323 ITR 166 (SC), as interpreted by the Hon'ble Karnataka High Court in *CIT v/s Yokogawa India Ltd.*, [2012] 204 Taxman 305 (Kar.).

11. The learned Departmental Representative, while agreeing with the propositions laid down by the Hon'ble Karnataka High Court, in its judgment cited supra wherein the Hon'ble Court has dealt with an identical issue and the same was decided in favour of the Revenue, relied on the provisions of section 36(1)(vii) of the Act, and submitted that the interpretation requires re-consideration. He further relied on Page-30, of the assessee's paper book and submitted that for the purpose of computation of managerial remuneration, the assessee has added back the provision for doubtful debts and advances to arrive at the profits. 12. In reply, the learned Counsel relied on the provisions of [section 309](#) of Companies Act, 1956, and submitted that the manner in which the net profits are to be computed for the purpose of calculation of ITA Nos. 2777/Mum/2016 2778/Mum/ 2016 A.Y. 2010-11 & 2011-12 remuneration of directors is specified and hence, the argument of the learned Departmental Representative is wrong. 13. After hearing rival contentions, we find that the assessee has debited the Profit & Loss Account by the amount of provisions for doubtful debts / advances. This appears in Schedule-I/Item-4(P) under the head "General Expenses". Thereafter, the assessee has reduced the provisions from the loans and advances appeared in Schedule-I of the Balance Sheet and from sundry debtors appearing in Schedule-G of the balance sheet. The Hon'ble Supreme Court in *Vijaya Bank v/s CIT*, [2010] 323 ITR 166 (SC), held as follows: - "However, if an assessee debits provision for doubtful debts to the profit and loss account and makes a corresponding credit to the "current liabilities and provisions" on the liabilities side of the balance sheet, then it would constitute a provision for doubtful debt. In the latter case, the assessee would not be entitled to deduction after April 1, 1989." 14. The Hon'ble Karnataka High Court in *Yokogawa India Ltd.* (supra) has relied on the judgment of Hon'ble Supreme Court in *Vijaya Bank* (supra), and at Page-310, the Hon'ble Supreme Court held as follows: -

5 However, it was clarified that besides debiting the profit and loss account and creating a provision for bad and doubtful debt, the assessee correspondingly/simultaneously obliterated the said provision from its accounts by reducing the corresponding amount from loans and advances/debtors on the assets side of the balance sheet and, consequentially, at the end of the year, the figure in the loans and advances or the debtors on the assets side of the balance sheet was shown as net of the provision for the impugned bad debt. Then the said amount representing bad debt or doubtful debt cannot be added in order to compute book profit. Therefore, after the Explanation the assessee is now required not only to debit the profit and loss account but simultaneously also reduce the loans and advances or the debtors from the assets side of the balance sheet to the extent of the corresponding amount so that, at the end of the year, the amount of loans and advances/debtors is shown as net of the provisions for the Impugned bad debt. Therefore, in the first place if the bad debt or doubtful debt is reduced from the loans and advances or the debtors from the assets side of the balance sheet the Explanation to Section ITA Nos. 2777/Mum/2016 2778/Mum/2016 A.Y. 2010-11 & 2011-12 115JA or JB is not at all attracted. In that context even if amendment which is made retrospective the benefit given by the Tribunal and the appellate Commissioner to the assessee is in no way affected. In that view of the matter, we do not see any merit in this appeal."

7. In view of the finding of the Hon'ble ITAT, we are of the view that the claim of the assessee is liable to be allowed in the interest of justice. No distinguishable material has been produced before us. The factual situation is also not the different of the case decided by Hon'ble ITAT (supra). The claim of the assessee has been decided by the Hon'ble ITAT by following the law settled by Hon'ble Supreme Court (Supra) and by the Hon'ble High Court of Karnataka (supra). Taking into account, all the facts and circumstances of the case, we decide this issue in favour of the assessee against the revenue."

6. Respectfully following the above decision of the Co-ordinate Bench, we are inclined to dismiss the ground No.2 raised by the Revenue.

7. In the net result, the appeal filed by the Revenue is dismissed.
Order pronounced in the open court on 02.06.2021

Sd/-
MAHAVIR SINGH
VICE PRESIDENT

Sd/-
S. RIFAUH RAHMAN
ACCOUNTANT MEMBER

MUMBAI, DATED: 02.06.2021

Copy of the order forwarded to:

- (1) The Assessee;
- (2) The Revenue;
- (3) The CIT(A);
- (4) The CIT, Mumbai City concerned;
- (5) The DR, ITAT, Mumbai;
- (6) Guard file.

Pradeep J. Chowdhury
Sr. Private Secretary

True Copy
By Order

Assistant Registrar
ITAT, Mumbai