

आयकर अपीलीय अधिकरण, 'ए' न्यायपीठ, चेन्नई।
IN THE INCOME TAX APPELLATE TRIBUNAL
'A' BENCH: CHENNAI
श्री वी दुर्गा राव, न्यायिक सदस्य एवं श्री जी मंजूनाथा, लेखा सदस्य के समक्ष
BEFORE SHRI V. DURGA RAO, JUDICIAL MEMBER AND
SHRI G. MANJUNATHA, ACCOUNTANT MEMBER

आयकर अपील सं./ITA No.3350/Chny/2018
निर्धारण वर्ष /Assessment Year: 2012-13

M/s. Tremco Roofing & Facility Services Pvt. Ltd.,
No.60, B-1, First Floor,
Ganesh Towers, First Avenue,
100 Feet Road, Ashok Nagar,
Chennai – 600 083.
[PAN: AADCT 5389H]
(अपीलार्थी/Appellant)

The Asst. Commissioner of Income Tax,
Vs. Corporate Circle-3(1),
Chennai.
(प्रत्यर्थी/Respondent)

अपीलार्थी की ओर से/ Appellant by : Shri Farookh Irani, Advocate
प्रत्यर्थी की ओर से /Respondent by : Shri S. Bharath, CIT
सुनवाई की तारीख/Date of Hearing : 25.10.2021
घोषणा की तारीख /Date of Pronouncement : 22.12.2021

आदेश / ORDER

Per V. Durga Rao, Judicial Member:

This appeal filed by the assessee is directed against the order of the Learned Commissioner of Income Tax (Appeals)-11, Chennai in I.T.A No.85/2016-17 dated 26.09.2018 relevant to the Assessment Year 2012-13.

2. The grounds of appeal raised by the assessee are as under:

“Based on the facts and in the circumstances of the case and in law, Tremco Roofing & Facility Services Private Limited (hereinafter referred to as 'the Appellant') craves leave to prefer an appeal against the order dated 26 September 2018

(received on 11 October 2018) passed by the Commissioner of Income-tax (Appeals) -11 [‘learned CIT(A)] under section 250 of the Income-tax Act, 1961 (‘Act’) on the following grounds:

Ground 1 - Disallowance of claim of provision for losses

1.1 Based on the facts and in the circumstances of the case and in law, the learned CIT(A) erred in upholding the disallowance of provision for losses amounting to Rs 12,31,40,818 by holding the same as contingent in nature even though the provision was made following Accounting Standard - 7.

1.2 Based on the facts and in the circumstances of the case and in law, the learned CIT(A) has failed to appreciate that disallowance of provision for losses results in taxability of income which does not exist thereby ignoring the principle of taxability and real income.

The Appellant craves leave to add, alter, omit or substitute any or all of the above grounds of appeal, at any time before or at the time of the appeal hearing.”

3. The brief facts of the case are that the assessee is a company, filed its return of income for the assessment year 2012-13 declaring total income of Rs. 1,25,40,710/-. The case was selected for scrutiny through CASS. After following due procedure, an assessment was completed. In the assessment order, on perusal of the financials of the assessee, the A.O has noted that the assessee had debited an amount of Rs.12,31,40,818/- to the P&L statement as provision for losses. The assessee was asked to explain the nature of the provision made and if any disallowance was made in the statement of income, given that the expenditure booked is only a provision and not an actual expenditure. The

assessee has explained that no disallowance was made but since the assessee has suffered losses, such a provision was made in the books. The Assessing Officer, however, not convinced with the computation of the assessee and according to the Assessing Officer, the amount debited to P&L account is on account of a provision and not an actual expenditure. The same is not in conformity with prudent accounting principles and does not depict a true picture of the income of the assessee. Hence, the said expenditure is disallowed and added back to income of the assessee.

4. On appeal before the Ld. CIT(A), the Ld. CIT(A) has noted that the A.O has disallowed the provision made by the assessee on the ground that it is not an actual expenditure and not in conformity with the prudent accounting principles. He further noted that the provisional and contingent losses cannot be allowed as expenditure in any earlier year prior to the same being fructified. In the instant case also, the assessee-company has claimed a loss of Rs. 12.31 crores on estimate basis when the losses are yet to arise to the assessee in the subsequent 3-4 years. The loss claimed by the assessee is a pre-mature, projected and contingent loss and thus, cannot be claimed as legitimate business expenditure. The *post-facto* events in the future years might have confirmed the projection of losses by the assessee. However, the losses cannot be allowed on a projected basis unless they are actually incurred and verifiable with proper

accounting methods. Hence, the Ld. CIT(A) confirmed the order of the A.O.

5. On being aggrieved, the assessee carried the matter before the Tribunal. The Id. counsel for the assessee has submitted that L&T was the main contractor of the Mumbai International Airport and the assessee was awarded the bid of construction of roofing vide agreement dated 6/9/2010 for roofing of the project of Mumbai International Airport Ltd.

5.1 The assessee has entered into a fixed price contract with L&T Ltd. for installing multi-phase roofing system installation at the Mumbai International Airport. The project commenced in August, 2010 and was expected to be executed over more than one accounting period. Due to various unforeseen events which occurred during the course of project execution, certain unplanned costs had to be incurred by the assessee to complete the project. These costs including significant increases in necessary material, labour and other costs to address these unplanned events. Given the fixed price nature of contract with L&T Ltd., the assessee has begun to incur significant losses on the project. These losses had majorly occurred during the financial year relevant to the assessment year 2012-13 and were appropriately provided for in the profit and loss account in accordance with Accounting Standard-7, which was consistently followed by Tremco India. Thus, both during the subject

assessment year and subsequent assessment years, the assessee actually incurred project losses, which is evident from the audited financial statements and accordingly, the assessee has made a provision for losses as per AS-7.

5.2 He further pointed out from the AS-7(21), against the contract revenue and expenses and recognition of expected losses, he submitted that when it is probable that total contract costs will exceed total contract revenue, the expected loss should be recognised as an expense immediately. He also pointed out from the paper book page No.53 that as per CBDT Circular No.9949, dated 21/01/1996, which provides that accounting policies adopted by an assessee should be such so as to represent a true and fair view of the state of affairs of the business, profession or vocation in the financial statements prepared and presented on the basis of such accounting policies. The major considerations governing the selection and application of accounting policies are the following namely: (i) Provisions should be made for all known liabilities and losses even though the amount cannot be determined with certainty and represents only a best estimate in the light of available information and submitted that the provisions for loss made by the assessee is also supported by the above CBDT circular, supra. He further relied on the following decisions namely:

1. *Rotork Controls India Private Limited vs CIT, Chennai (2009) 180 taxman 422 (SC);*
2. *CIT vs Woodward Governor India Private Limited (2009) 179 Taxman 326;*
3. *Jacobs Engineering India Pvt. Ltd. vs ACIT (2011) 14 taxmann.com 186 (Mumbai Tribunal);*
4. *Dredging International N.V. vs ADIT (2011) 48 SOT 430 (Mumbai Tribunal);*
5. *Mazagon Dock Ltd vs JCIT (2009) 29 SOT 356 (Mumbai Tribunal);*
6. *ACIT vs Triveni Engineering & Industries (ITA 346 of 2009) (Delhi HC);*
7. *ACIT vs M/s ITD Cementation India Ltd (ITA 2991/Mum/2011) (Mumbai Tribunal);*
8. *ACIT vs Ashoka Buildcon Ltd (ITA 394/PN/2007) (Pune Tribunal);*
9. *Bharat Earth Movers vs CIT (2000) 112 Taxman 61 (SC);*
10. *CIT vs Metal Box India Ltd (192) 63 taxman 160 (Cal. HC);*
11. *Calcutta Co Ltd vs CIT [1959] 37 ITR 1 (SC);*
12. *ITO vs Andhra Pradesh Paper Mills Ltd (1991) 38 ITD 1 (Hyderabad Special Bench);*
13. *Kedarnath Jute Mfg. Co. Ltd vs CIT (1971) 82 ITR 363 (SC);*
14. *Principal CIT vs Haryana warehousing Corporation (2017) 77 taxmann.com 43 (Punjab & Haryana HC).*

The Id. Counsel for the assessee has submitted that the provision made by the assessee is as per AS-7 and also CBDT Circular, supra, and further based on the judicial precedence. Therefore, he submitted, the provisions for the loss booked by the assessee may be allowed.

6. On the other hand, the Id. Departmental Representative has submitted that the assessee has not submitted any scientific method before the A.O that the loss is estimated by the assessee. He further

submitted that the assessment year under consideration, the assessee has made a huge profit therefore the assessee instead of paying taxes for the year under consideration shifted to subsequent years and he strongly supported the orders passed by the other authorities below.

7. We have heard both the sides, perused the materials available on record and gone through the orders of authorities below including case law relied on by the Id. Counsel for the assessee. The case of the Assessing Officer is that the assessee has debited an amount of ₹.12,31,40,818/- to the profit and loss account as a provision of losses. Before the Assessing Officer, the assessee has not explained the basis for the provision of losses. Therefore, the Assessing Officer has disallowed the same. On appeal, the Id. CIT(A) confirmed the order of the Assessing Officer.

7.1 In this case, we find that the assessee has not given any scientific basis for the provision made either before the Assessing Officer or before the Id. CIT(A) or even before the Tribunal. The main argument of the assessee is that due to various unforeseen events which occurred during the course of project execution, certain unplanned costs had to be incurred by the assessee to complete the project. These costs including significant increases in material, labour and other costs to address these unplanned events, the provision of loss has been created. This is the only

submission made before us. The above submission was neither placed before the Assessing Officer nor before the Id. CIT(A). In so far as the above statement is concerned, the Id. Counsel has not explained any basis as to how the material cost and labour cost are increased. Except stating the above, the Id. Counsel for the assessee has not explained any scientific basis for which the assessee is going to incur such huge expenditure of ₹.12.31 crores as a loss.

7.2 We find that there is no change in the terms and conditions of the contract entered into and subsequently executed and same amount has been received. The assessee has not placed any material on record to show that any increase in the cost of material and cost of labour and other services to anticipate future loss. Apart from the above, the assessee has not incurred any loss and the assessee gain profit much more in the subsequent years. In fact, the assessee reversed the provision made in this year under consideration in subsequent two financial years. Therefore, the above facts clearly show that there is no basis for the assessee to make the provision and it is only an estimation made by the assessee.

7.3 The Id. Counsel has also submitted that the provision made by the assessee is supported by Accounting Standard 7. We have gone through the Accounting Standard 7, which has no application to the facts of the

assessee's case. Even the CBDT circular relied on by the assessee has no application to the facts of the present case.

8. In so far as the case law relied on by the Id. Counsel for the assessee, in the case of Rotork Controls India Private Limited v. CIT (supra), the assessee sold valve actuators. At the time of sale, the assessee provided standard warranty that if the product was defective within the stated period, the product would be rectified or replaced free of charge. For AY 1991-92, the assessee made a provision for warranty at Rs.10,18,800/- at the rate of 1.5% of the turnover. As the actual expenditure was only Rs.5,18,554/-, the excess provision of Rs.5,00,246/- was reversed and only the net provision was claimed. The Tribunal allowed the claim on the basis that the provision had been consistently made and on a realistic manner, which was upheld by the Hon'ble Supreme Court by reversing the decision of the Hon'ble High Court. In this case, the Tribunal has held that right from the assessment year 1983-84 the CIT (A) as well as the Tribunal had allowed the warranty claim(s) on the ground that Valve Actuators are sophisticated equipments; that in the course of manufacture and sale of Valve Actuators a reasonable warranty was given to the purchasers; that every item of sale was covered by the warranty scheme; that no purchaser was ready and willing to buy Valve Actuators without warranty and consequently every item sold had a

corresponding obligation under the warranty clause(s) attached to such sales.

In the above case, the provision made are for warranty and the same was made in realistic manner and therefore, the Hon'ble Supreme Court upheld the scientific method adopted by the assessee. In the present case, no scientific method was adopted by the assessee to estimate the loss. Therefore, the case law relied on by the assessee has no application to the facts of the present case.

8.1 In the case of CIT v. Woodward Governor India Private Limited (supra), the substantial question of law arises for determination before the Hon'ble Supreme Court are (i) Whether, on the facts and circumstances of the case and in law, the additional liability arising on account of fluctuation in the rate of exchange in respect of loans taken for revenue purposes could be allowed as deduction under Section 37(1) in the year of fluctuation in the rate of exchange or whether the same could only be allowed in the year of repayment of such loans? and (ii) Whether the assessee is entitled to adjust the actual cost of imported assets acquired in foreign currency on account of fluctuation in the rate of exchange at each balance sheet date, pending actual payment of the varied liability? This case is relating to foreign exchange fluctuation and the facts are

entirely different from the case in hand and no application to the facts of the assessee's case.

8.2 In the case of *Bharat Earth Movers v. CIT (supra)*, the Hon'ble Supreme Court satisfied that provision made by the appellant company for meeting the liability incurred by it under the leave encashment scheme proportionate with the entitlement earned by employees of the company, inclusive of the officers and the staff, subject to the ceiling on accumulation as applicable on the relevant date, is entitled to deduction out of the gross receipts for the accounting year during which the provision is made for the liability. In this case, the Hon'ble Supreme Court has held that if a business liability is arised in the accounting year, deduction should be allowed although the liability may be quantified and discharged at a future date, but, what should be definition is incurring of liability. In the present case, the loss claimed by the assessee is not a definite and it is only an estimate. Therefore, the case law relied on by the assessee has no application to the facts of the present case.

8.3 Similarly, other case law relied on by the Id. Counsel for the assessee also has no application to the facts of the present case. In this case, the estimation of future loss was neither based on any actuarial or any scientific method of determination of its liability and thus, we confirm the orders of authorities below that the losses could not be allowed on a

projected basis unless they are actually incurred and verifiable with proper accounting methods. Thus, the ground raised by the assessee stands dismissed.

9. In the result, the appeal filed by the assessee is dismissed.

Order pronounced on 22nd December, 2021 in Chennai.

Sd/-

(श्री जी मंजूनाथा)

(G. MANJUNATHA)

लेखा सदस्य/ACCOUNTANT MEMBER

Sd/-

(वी दुर्गा राव)

(V. DURGA RAO)

न्यायिक सदस्य/JUDICIAL MEMBER

चेन्नई/Chennai, दिनांक/Dated: 22nd December, 2021.

EDN/-

आदेश की प्रतिलिपि अग्रेषित/**Copy to:**

1. अपीलार्थी/Appellant
2. प्रत्यर्थी/Respondent
3. आयकर आयुक्त (अपील)/CIT(A)
4. आयकर आयुक्त/CIT
5. विभागीय प्रतिनिधि/DR
6. गार्ड फाईल/GF