

IN THE INCOME TAX APPELLATE TRIBUNAL
DELHI BENCH : C : NEW DELHI

BEFORE SHRI R.K. PANDA, ACCOUNTANT MEMBER
AND
MS SUCHITRA KAMBLE, JUDICIAL MEMBER

ITA No.502/Del/2018
Assessment Year: 2013-14

Helti India Pvt. Ltd.,
6th Floor, Building 8, Tower C,
DLF Cyber City, Phase 3,
Gurgaon.

Vs Addl. CIT,
Special Range-4,
New Delhi.

PAN: AAACH3583Q

(Appellant)

(Respondent)

Assessee by	:	Shri S.K. Aggarwal, CA
Revenue by	:	Shri Kumar Padmapani Bora, Sr. DR
Date of Hearing	:	16.11.2021
Date of Pronouncement	:	14.02.2022

ORDER

PER R.K. PANDA, AM:

This appeal filed by the assessee is directed against the order dated 31.10.2017 of the CIT(A)-35, New Delhi, relating to AY 2013-14.

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

õGeneral

1. That based on the facts and circumstances of the case and in law, the Ld. CIT(A) has erred in confirming disallowance of Rs. 24,69,085/- in terms of order dated November 02, 2016 passed under section 143(3) of the Act (hereinafter referred as 'impugned assessment order') by the Addl. Commissioner of Income-tax, Special Range-4, New Delhi (Ld. AO).

Disallowance of Provision for settlement with the leasing company

2. That on the facts and circumstances of the case and in law, the Ld. CIT(A) has erred in restricting the claim of deduction to Rs. 10,30,915/- as against Rs. 35,00,000/- claimed by the Appellant towards loss arising on settlement of claim with the leasing company.

3. That on the facts and circumstances of the case and in law, the Ld. CIT(A) has erred in holding that the above claim of the Appellant, to the extent of Rs. 24,69,085/- is unascertained liability.

4. That on the facts and circumstances of the case and in law, the Ld. CIT(A) has erred in not appreciating:

- that the Appellant was consistently following mercantile system of accounting;

- that the above loss was incurred during the year under appeal on account of fraud undertaken by the employee.

- that the above loss was quantified based on reasonable estimate on the basis of material / information available with the Appellant.

5. That on the facts and circumstances of the case and in law, the Ld. CIT(A) has erred in not adjudicating the following specific ground of appeal taken by the Appellant:

öwithout prejudice to the above, in an unlikely situation of upholding the disallowance of the aforesaid provision of Rs 35,00,000 in AY 2013-14, the Appellant should be allowed deduction of the said amount of Rs 35,00,000 subsequent AY(s), when the settlement was finally completedö

The above, grounds of appeals are without prejudice to and independent of one another.

The Appellant craves leave to amend, modify, rescind, supplement or alter or add any of the grounds stated herein above, either before or at the time of hearing of this appeal.

The Appellant prays for relief based on the said grounds of appeal and the facts and circumstances of the case.ö

3. Facts of the case, in brief, are that the assessee is a company and engaged in the business of trading of construction, engineering and technical tools and equipments. It filed its return of income on 29.11.2013 declaring an income of Rs.7,13,69,375/-. During the course of assessment proceedings, the AO noted that the Note No.41 of the note of accounts attached to the audited financial statement provides that the assessee has created a provision of Rs.35 lakhs on account of settlement with the leasing companies for a fraud committed by one of the employees of the company. He, therefore, asked the assessee to furnish the complete details of this provision and asked the assessee to explain as to why this amount should be allowed as a deduction.

3.1 The assessee, in its reply, submitted that during the year the company was defrauded by one of its employees who sold the vehicles hired by the company on lease charges basis. On realization of the fraud, the company initiated legal action against the employee. However, in relation to the loss caused to the leasing company, the same was required to be indemnified by the company for which the provision of Rs.35 lakhs was made in the books of account. It was argued that eventually the amount was settled with the leasing company at Rs.39,92,063/- out of which Rs.10,30,915/- was paid on 30th March, 2013 and the balance was paid during the FY 2013-14.

3.2 However, the AO was not satisfied with the arguments advanced by the assessee and made an addition of Rs.35 lakhs by observing as under:-

õ6. As per the provision of Income Tax Act, only the expenditure incurred for the purposes of business of the assessee can be allowed as deduction u/s 37 of the Income Tax Act. Further, no deduction towards the provisions for unascertained liability is allowable. The documents furnished by the assessee suggest that in this case an FIR was filed on 27/08/2013 with Police Station, Okhla Industrial Area, New Delhi. This FIR explains the nature of fraud and also mention that till 27/08/2013 the company paid total sum of Rs.' 17,13,638/- towards partial settlement of the claim of leasing companies. As against this, the assessee company has filed a copy of letter dated 31/08/2013 addressed to SFIO, Okhla Industrial Area which mentions that the assessee has already settled the payment to the leasing companies by paying Rs. 39,92,063/- and these payments were made by 18.6.2014. Both these documents have been filed by the assessee which contradict each other. It appears from these documents that the company was required to make the settlement with the leasing companies but the quantum of settlement was not fixed. Since, in the FIR dated 27/08/2013, the amount paid on account of settlement is mentioned as Rs, 17,13,638/- therefore, the provision of Rs. 35,00,000/- created in the financial year 2012-13 amounts to provision for unascertained liabilities. As the provision of 35,00,000/- was on account of unascertained liability, the same cannot be allowed as deduction as claimed by the assessee. Accordingly, an amount of Rs. 35,00,000/- is being added back to the income of the assessee.ö

4. In appeal, the Id. CIT(A) allowed benefit of Rs.10,30,915/- and sustained the balance amount by observing as under:-

õ4.2.3. The submissions of the appellant, the case laws cited and the relevant order have been considered. In the present case, only the expenditure incurred for the purposes of business of the Appellant can be allowed as deduction U/s 37 and no deduction towards the provision for unascertained liability is allowable under the Income Tax Act. As the provision of 35,00,000/- was on account of unascertained liability, the same cannot be allowed as a deduction as claimed by the Appellant. I find no reason to interfere with the AO's order on this issue. However, the appellant has paid Rs.10,30,915/- towards the settlement during A.Y. 2013-14 and the same is allowed as expense incurred for business purposes. Ground nos. 1 & 2 are partly allowed.ö

5. Aggrieved with such order of the CIT(A), the assessee is in appeal before the Tribunal.

6. The ld. Counsel for the assessee, referring to Note 41 to the financial statements for the year ended 31st March, 2013 placed at page 58 of the paper book, drew the attention of the Bench to the same which reads as under:-

ö41. During the year the company has reported a fraud, done by an employee of the company on account of cars hired by the Company on lease charges basis. Even though the Company has filed legal action against the said employee, the issue has been settled with the leasing books of accounts as on 31st March, 2013.ö

7. He submitted that the estimate made by the assessee is on fair and reasonable basis and the liability is ascertainable the moment it is incurred. He submitted that in the instant case, the assessee has filed an FIR on 27th August, 2013, copy of which is placed at pages 116 to 120 of the paper book. He submitted that the assessee in its accounts has shown this liability on estimate basis which was reasonable under the facts and circumstances of the case and the assessee is following mercantile system of accounting. Therefore, it was incumbent upon the assessee to show the same on accrual basis. Referring to the decision of the Honöble Supreme Court in the case of Bharat Earth Movers vs. CIT, reported in 112 taxman 61, he submitted that the Honöble Supreme Court in the said decision has held that if a business liability has definitely arisen in the accounting year, deduction should be allowed although the liability may have to be quantified and discharged at a future date. What should be certain is the incurring of the liability and it should be capable of being estimated with reasonable certainty though the actual quantification may not be possible. If these requirements are satisfied the

liability is not a contingent one. The liability is in praesenti though it will be discharged at a future date. It does not make any difference if the future date on which the liability shall have to be discharged is not certain.

8. Referring to the decision of the Honøble Delhi High Court in the case of CIT vs. Vodafone Essar South Ltd., reported in 230 Taxman 541, he submitted that the Honøble High Court in the said decision has held that where the assessee follows mercantile system of accounting expenses due and payable should be allowed as an expenditure is not confined only to the money actually paid towards the liability, but, also covers a liability to accrue although discharge could be at a future date. Referring to the following decisions, he submitted that similar view has been taken in these decisions also:-

- (i) Canara Housing Development Company v. Joint Commissioner of Income-tax, (OSD) [2017] 81 taxmann.com 472 (Bangalore-Trib.);
- (ii) R.C. Gupta v. Commissioner of Income-tax, Delhi-VIII [2008] 166 Taxman 191 (Delhi);
- (iii) Neyveli Lignite Corporation Ltd. v. Assistant Commissioner of Income-tax [2005] 2 SOT 863 (Chennai);
- (iv) Deputy Commissioner of Income-tax, Circle - 11(1), New Delhi v. EDS Electronics Data Systems (India) (P.) Ltd. [2008] 20 SOT 403 (Delhi);

- (v) Oriental Insurance Co. Ltd. v. Joint Commissioner of Income-tax, SR-4, New Delhi [2007] 12 SOT 432 (Delhi);
- (vi) TRF Ltd. v. Commissioner of Income-tax, Ranchi [2011] 11 taxmann.com 235 (Jharkhand); and
- (vii) Hoechst Marion Roussel Ltd. v. Joint Commissioner of Income-tax, SR-34, Mumbai [2007] 16 SOT 15 (Mumbai).

9. He submitted that the assessee, in the instant case, has made reasonable estimates and, therefore, the Id.CIT(A) was not justified in restricting the claim to Rs.10,30,915/- as against Rs.35 lakhs claimed by the assessee.

10. The Id. DR, on the other hand, heavily relied on the order of the CIT(A).

11. We have heard the rival arguments made by both the sides, perused orders of the AO and the CIT(A) and the paper book filed on behalf of the assessee. We have also considered the various decisions cited before us. We find, the AO, in the instant case, disallowed the provision of Rs.35 lakhs made by the assessee on account of settlement with the leasing company on the ground that no deduction towards the provision for unascertained liability is allowable. According to the AO, the assessee has only filed an FIR and the copy of the FIR mentions that the assessee has already settled the payments with the leasing company by paying Rs.39,92,063/- and this payment was made on 18th June, 2014. According to the AO, these documents filed by the assessee contradict with each other. Since the

provisions of Rs.35 lakh was on account of unascertained liability, he disallowed the same. We find, the Id.CIT(A) allowed an amount of Rs.10,30,915/- and disallowed the balance amount, the reasons of which have already been reproduced in the preceding para. It is the submission of the Id. Counsel for the assessee that the liability is allowable the moment it was incurred and the estimate made by the assessee was fair and reasonable. Since the assessee is following mercantile system of accounting, therefore, in relation to the loss caused to the leasing company which was to be indemnified by the assessee company, the provision for Rs.35 lakhs was made in the books of account which was fair and reasonable.

11.1 We find force in the above argument of the Id. Counsel. The Hon^{ble} Supreme Court in the case of Bharat Earth Movers (supra), reported in 245 ITR 428, at paras 4 to 7 of the order has observed as under:-

4. The law is settled: if a business liability has definitely arisen in the accounting year, the deduction should be allowed although the liability may have to be quantified and discharged at a future date. What should be certain is the incurring of the liability. It should also be capable of being estimated with reasonable certainty though the actual quantification may not be possible. If these requirements are satisfied the liability is not a contingent one. The liability is in praesenti though it will be discharged at a future date. It does not make any difference if the future date on which the liability shall have to be discharged is not certain.

5. In Metal Box Company of India Ltd. Vs. Their Workmen (1969) 73 ITR 53 the appellant company estimated its liability under two gratuity schemes framed by the company and the amount of liability was deducted from the gross receipts in the P&L account. The company had worked out on an actuarial valuation its estimated liability and made provision for such liability not all at once but spread over a number of years. The practice followed by the company was that every year the company worked out the additional liability incurred by it on the employees putting in every additional year of service. The gratuity was payable on the termination of

an employees service either due to retirement, death or termination of service ó the exact time of occurrence of the latter two events being not determinable with exactitude before hand. A few principles were laid down by this court, the relevant of which for our purpose are extracted and reproduced as under :-

(i) For an assessee maintaining his accounts on mercantile system, a liability already accrued, though to be discharged at a future date, would be a proper deduction while working out the profits and gains of his business, regard being had to the accepted principles of commercial practice and accountancy. It is not as if such deduction is paid; permissible only in case of amounts actually expended or

(ii) Just as receipts, though not actual receipts but accrued due are brought in for income-tax assessment, so also liabilities accrued due would be taken into account while working out the profits and gains of the business;

(iii) A condition subsequent, the fulfillment of which may result in the reduction or even extinction of the liability, would not have the effect of converting that liability into a contingent liability;

(iv) A trader computing his taxable profits for a particular year may properly deduct not only the payments actually made to his employees but also the present value of any payments in respect of their services in that year to be made in a subsequent year if it can be satisfactorily estimated.

6. So is the view taken in *Calcutta Co. Ltd. Vs. Commissioner of Income-Tax, West Bengal* (1959) 37 ITR 1 wherein this court has held that the liability on the assessee having been imported, the liability would be an accrued liability and would not convert into a conditional one merely because the liability was to be discharged at a future date. There may be some difficulty in the estimation thereof but that would not convert the accrued liability into a conditional one; it was always open to the tax authorities concerned to arrive at a proper estimate of the liability having regard to all the circumstances of the case.

Applying the above-said settled principles to the facts of the case at hand we are 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. The liability is not a contingent liability. The High Court was not right in taking the view to the contrary.

7. The appeal is allowed. The judgment under appeal is set aside. The question referred by the Tribunal to the High Court is answered in the affirmative, i.e. in favour of the assessee and against the Revenue.ö

12. We find, the Honøble Delhi High Court in the case of CIT vs. Vodafone Essar South Ltd. (supra), has held as under:-

ö10. The first appellate authority has observed that the expenditures should not be allowed as it had not been incurred but only a provision has been made. He further held that the provisions were for non-existing liabilities which had not been quantified. On the other hand, the finding of the Tribunal is to the contrary. Before us, the Revenue has not filed copy of the documents or papers, which were filed by the assessee in support of their contentions and to negate and challenge the findings of the Tribunal that the amounts claimed as expenses were not provisions in the sense that no services had been rendered and the expenditure had not been incurred. The finding of the Tribunal is clearly that relevant bills had not been received but the services had been rendered and tasks performed. The expenditure was incurred. In view of the aforesaid position, we are not inclined to interfere on the first aspect/question raised by the Revenue.

11. The undisputed position is that the assessee follows mercantile system of accountancy. The term "expenditure" donates idea of spending, paying out or away; it is something which is gone irretrievably. ([See Indian Molasses Co. \(P\) Ltd. v. CIT](#), (1959) 37 ITR 66). In mercantile system the term expenditure is not necessarily confined to money actually paid towards a liability, but would cover a liability accrued or has been incurred in praesenti, although the discharge could be at a future date. A liability accrues or is incurred when it is an ascertained liability and not a contingent liability, i.e. liability which may or may not accrue and is uncertain. A liability, which actually exists and is also not disputed by assessee, but merely not paid, is not a contingent liability when the work or obligation has been actually performed by the third party to whom the payment is due. When the assessee accepts performance of the work or obligation and accepts liability to pay, it partake the character of actual liability in praesenti and is not dependent upon future happening of an event, which would result in creation of liability subsequently. In the former cases, the liability has incurred or accrued, but actual payment remains unpaid and would be made in the next year(s). Off course, the assessing officer can examine and go into valuation of the liability and decide whether it has been satisfactorily and fairly determined.

12. Assessing Officer and Appellate Authority in their orders had primarily relied upon the terminology or nomenclature of "provision" to disallow the

claim of expenditure of Rs 29,90,064/- and Rs 28,62,275/- and opine that the provisions made should not be treated as expenditure incurred. This is not the correct and true test, which is to be applied. A "provision" can be made in respect of amounts which have become due and payable in the relevant previous year and therefore could be debited to the profit and loss account, once they represent ascertained liability. We do not find any negative elucidation on the relevant aspects in the orders passed by Assessing Officer and the C.I.T (Appeals). Albeit, there is elucidation and finding recorded by tribunal that the services had actually been performed and liability was accepted by the respondent assessee. The amounts therefore represented ascertained liabilities. These were shown as "provisions" as the services were rendered close to the assessment years and relevant bills had not been received. This would not make the provisions a contingent liability.

13. Appropriate would be to refer to the decision of the Supreme Court in Calcutta Company Ltd. Vs. Commissioner of Income Tax, West Bengal, (1959) 37 ITR 1, wherein it was held that if liability has been definitely incurred in form of unconditional contractual liability, it would not become contingent because payment has to be paid in future. However, liability should have been fairly and accurately estimated. The following passage from the said decision is relevant:-

"Turning now to the facts of the present case, we find that the sum of Rs. 24,809 represented the estimated expenditure which had to be incurred by the appellant in discharging a liability which it had already undertaken under the terms of the deeds of sale of the lands in question and was an accrued liability which according to the mercantile system of accounting the appellant was entitled to debit in its books of account for the accounting year as against the receipts of Rs. 43,692-11-9 which represented the sale proceeds of the said lands. Even under [s. 10\(2\)](#) of the Income-tax Act, it might possibly be urged that the word "expended" was capable of being interpreted as "expendable" or "to be expended" at least in a case where a liability to incur the said expenses had been actually incurred by the assessee who adopted the mercantile system of accounting and the debit of Rs. 24,809 was thus a proper debit in the present case. We need not however base our decision on any such consideration. We are definitely of opinion that the sum of Rs. 24,809 represented the estimated amount which would have to be expended by the appellant in the course of carrying on its business and was incidental to the same and having regard to the accepted commercial practice and trading principles was a deduction which, if there was no specific provision for it under [section 10\(2\)](#) of the Act was certainly allowable deduction, in arriving at the profits and gains of the business of the appellant under [section 10\(1\)](#) of the Act, there being no prohibition against it, express or implied in the Act.

It is to be noted that the appellant had led evidence before the Income-tax authorities in regard to this estimated expenditure of Rs. 24,809 and no exception was taken to the same in regard to the quantum, though the permissibility of such a deduction was questioned by them relying upon the provisions of [s. 10\(2\)](#) of the Act.

It therefore follows that the conclusion reached by the High Court in regard to the disallowance of Rs. 24,809 was wrong and it should have answered the referred question in the affirmative."

14. The aforesaid principles were applied to allow deduction of "provision" for gratuity, in case of serving employees and to whom the gratuity was payable only on retirement/termination, subject to condition that the amount so estimated was sufficiently certain to be capable of being valued. Gratuity payable in future, it has been held, was an obligation arising out of the present engagement and the estimated liability was ascertainable. As a present obligation, it could be allowed as a deduction in the profit and loss account. Subsequently, [Section 40A\(7\)](#) of the Act was enacted to specify and stipulate that provision for gratuity would be allowed in the profit and loss account when additional conditions stated therein were also satisfied. [See decision of the Supreme Court in [Shree Sajjan Mills Ltd. v. CIT](#), (1985) 156 ITR 585 (SC)]

15. Again in [Bharat Earth Movers v. CIT](#) (2000) 245 ITR 428 (SC), it has been observed:-

"The law is settled: If a business liability has definitely arisen in the accounting year, the deduction should be allowed although the liability may have to be quantified and discharged at a future date. What should be certain is the incurring of the liability. It should also be capable of being estimated with reasonable certainty though the actual quantification may not be possible. If these requirements are satisfied the liability is not a contingent one. The liability is in present though it will be discharged at a future date. It does not make any difference if the future date on which the liability shall have to be discharged is not certain. ... A few principles were laid down by this court, the relevant of which for our purpose are extracted and reproduced as under:

(i) For an assessee maintaining his accounts on the mercantile system, liability already accrued, though to be discharged at a future date, would be a proper deduction while working out the profits and gains of his business, regard being had to the accepted principles of commercial practice and accountancy. It is not as if such deduction is permissible only in the case of amounts actually expended or paid ;

(ii) Just as receipts, though not actual receipts but accrued due are brought in for income-tax assessment, so also liabilities accrued due would be taken into account while working out the profits and gains of the business;

(iii) A condition subsequent, the fulfilment of which may result in the reduction or even extinction of the liability, would not have the effect of converting that liability into a contingent liability ;

(iv) A trader computing his taxable profits for a particular year may properly deduct not only the payments actually made to his employees but also the present value of any payments in respect of their services in that year to be made in a subsequent year if it can be satisfactorily estimated."

13. The various other decisions relied on by the Id. Counsel in the paper book also supports its case. In view of the above discussion and respectfully following the decisions cited above, we are of the considered opinion that the assessee is entitled to deduction of Rs.35 lakhs being the provision created on account of fraud committed by one of its employees which caused loss to the leasing company. We, therefore, set aside the order of the CIT(A) and direct the AO to allow the deduction of Rs.35 lakhs in full.

14. In the result, the appeal filed by the assessee is allowed.

Order pronounced in the open court on 14th February, 2022.

Sd/-

(SUCHITRA KAMBLE)
JUDICIAL MEMBER

Sd/-

(R.K. PANDA)
ACCOUNTANT MEMBER

Dated: 14th February, 2022.

dk

Copy forwarded to :

1. Appellant
2. Respondent
3. CIT
4. CIT(A)
5. DR

Asstt. Registrar, ITAT, New Delhi