आयकर अपीलीय अधिकरण न्याय पीठ रायपुरमें।
IN THE INCOME TAX APPELLATE TRIBUNAL,
RAIPUR BENCH, RAIPUR

(Through Virtual Court)

BEFORE SHRI RAVISH SOOD, JUDICIAL MEMBER
AND
SHRI JAMLAPPA D BATTULL, ACCOUNTANT MEMBER

आयकर अपील सं. / ITA No. 306/RPR/2016

<u>निर्धारण वर्ष / Assessment Year : 2012-13</u>

Sri Jagannath Transport Corporation
2, Krishna Complex, Kuthchery Chowk,
Raipur (C.G.).
PAN : AACFJ3511F

.....अपीलार्थी / Appellant

बनाम / V/s.

The Assistant Commissioner of Income Tax,
Circle-3(1), Raipur (C.G.)

……प्रत्यर्थी / Respondent

Assessee by : Shri Veekaas S. Sharma, AR
Revenue by : Shri Sanjay Kumar, DR

सुनवाई की तारीख / Date of Hearing :15.03.2022
घोषणा की तारीख / Date of Pronouncement : 30.03.2022

आदेश / ORDER

PER RAVISH SOOD, JM:

The present appeal filed by the assessee is directed against the order passed by the CIT(Appeals)-1, Raipur, dated 01.04.2016, which in turn arises from the order passed by the A.O under Sec.143(3) of the Income-tax Act, 1961 (in short 'the Act'), dated 25.02.2015 for assessment year 2012-13. Before us the assessee has assailed the impugned order on the following grounds of appeal:

> "1. On the facts and in the circumstances of the case, the Learned AO has erred in facts and in law in disallowing Rs.81,350/- out of travelling expenses on account of alleged unsubstantiated personal element which is wholly arbitrary, baseless and unjustified and the Learned CIT(A) has erred on facts and in law in confirming the said disallowances.
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> 2. On the facts and in the circumstances of the case, the Learned AO has erred in facts and in law in disallowing Rs.2,38,087/- on account of penalty expenses without considering the nature of expenditure not being penalty for breach of provisions of law, which is wholly arbitrary, baseless and unjustified and the Learned CIT(A) has erred on facts and in law in confirming the said disallowance.
>
> 3. The Appellant craves leave to add, amend, alter and /or withdraw any or all the above grounds of appeal."

2. Controversy involved in the present appeal hinges around two issues, viz. (i). that as to whether or not the lower authorities are right in law and facts of the case in disallowing the assessee's claim for

deduction of Rs.2,38,087/-; and (ii). that as to whether the ad-hoc disallowance of travelling expenses of Rs. 81,350/- made by the A.O is sustainable in the eyes of law.

3. Shorn of unnecessary details, the assessee firm which is engaged in the business of a transport contractor had in its Profit & loss account debited an amount of Rs. 2,38,087/- under the head "Penalty". Holding a conviction that the assessee's claim for deduction of penalty militated against the 'Explanation-1' to Sec. 37(1) of the Act, the Assessing Officer disallowed the same. Also, the A.O being of the view that involvement of personal element could not be ruled out qua the assessee's claim for deduction of travelling expenses, thus, on an ad-hoc basis disallowed an amount of Rs. 81,350/- out of the same.

4. Aggrieved, the assessee carried the matter in appeal before the CIT (Appeals), but without any success.

5. The assessee being aggrieved with the order of the CIT (Appeals) has carried the matter in appeal before us.

6. Before us, it is the claim of the Ld. Authorized Representative (for short 'AR') for the assessee, that the lower authorities by merely being guided by the nomenclature of the assesee's claim for deduction of Rs. 2,38,087/- that was debited in its Profit & loss a/c under the head "Penalty" had wrongly disallowed the same by triggering "Explanation-1" to Section 37(1) of the Act. Elaborating on his aforesaid contention, it was submitted by the Ld. AR that the assessee's claim for deduction of an amount of Rs.2,38,087/- (supra) was in sum and substance an amount that was borne by the assessee firm, for the reason, that it had failed to execute certain contracts within the time period stipulated in the respective contracts. In order to fortify his aforesaid claim the Ld. AR had drawn our attention to the respective "memorandum of payments" evidencing payments of Rs.90,000/- and Rs.19,610/-. Backed by the aforesaid facts, it was submitted by the Ld. AR that as the payments in question were made by the assessee on account of infringement of the terms of contract, i.e, failure on its part to execute the respective contracts within the stipulated time period, and thus, were merely compensatory in nature,

therefore, the same were allowable as a deduction under Sec. 37(1) of the Act. It was submitted by the Ld. AR that its aforementioned claim for deduction was not hit by "Explanation-1" to Section 37(1) of the Act. On a specific query by the bench that the aggregate of the aforesaid payments worked out at Rs.1,09,061/- [Rs.90,000/- (+) Rs.19,610/-] as against the disallowance of an amount of Rs.2,38,087/- (supra) that was claimed by the assessee as a deduction, it was fairly admitted by the Ld. AR that documents corroborating its claim for deduction could only be gathered to the said extent. It was submitted by the Ld. AR that the balance amount of the impugned penalty was also in the nature of compensatory payments that were borne by the assessee for delay in meeting out its contractual obligations. Backed by his aforesaid contentions, it was the claim of the Ld. AR that the disallowance of Rs.2,38,087/- (supra) made by the Assessing Officer be vacated. Apropos the disallowance of an amount of Rs. 81,350/- out of travelling expenses i.e, on an ad hoc basis, it was submitted by the ld. AR that the A.O had neither specified any such expense which was allegedly held to be personal in nature,

nor given any sound basis for quantification of the said disallowance. Backed by his aforesaid contention, it was submitted by the ld. AR that the disallowance of travelling expenses not being backed by any concrete basis which would irrefutably support the same, thus, could not be sustained and was liable to be vacated.

7. Per contra, the Ld. Departmental Representative (for short 'DR') relied on the orders of the lower authorities.

8. We have heard the Ld. Authorized Representatives of both the parties, perused the orders of the lower authorities and the material available on record, as well as considered the judicial pronouncements that have been pressed into service by the Ld. AR to drive home his contentions. We shall first deal with the averrment of the ld. A.R that the lower authorities by misconceiving the assessee's claim for deduction of an amount of Rs. 2,38,087/- (supra) had wrongly disallowed the same. After having given a thoughtful consideration to the contentions advanced by the Ld. AR, we are principally in agreement with him that payments made by an assessee, though

dubbed as a penalty, but in substance being in the nature of compensatory payments borne by the assessee for having delayed the execution of a contract work, not being in the nature of an expenditure that was incurred for any purpose which was either an offence or, prohibited by law would not be hit by the "Explanation-1" to Sec. 37(1) of the Act. Admittedly, at the first glance the assessee's claim for deduction appeared to be towards discharge of a penalty, but then considering the substance of the liability leading to the said payments, we find that the same are in the nature of compensatory payments which the assessee had to bear on account of its failure to execute the respective contracts within the stipulated time period i.e, as per the terms of the contract. As per "Explanation-1" to Section 37(1) of the Act, where the assessee had incurred an expenditure for any purpose which is an offence; or which is prohibited by law, then, the same shall not be deemed to have been incurred for the purpose of business or profession and no deduction or allowance of the same shall be made while computing his income. However, in the case before us, we find that the payments/deductions in question are not in the nature of an

expenditure that was incurred/borne by the assessee for a purpose which was in the nature of an offence or, prohibited by law. On the contrary, as observed by us hereinabove, the payments in question are simpliciter in the nature of compensatory payments which had to be borne by the assessee for having failed to discharge its contractual obligations within the stipulated time period. In our considered view, as the respective payments i.e, to the extent of Rs. 1,09,610/- [Rs. 90,000/- (+) Rs. 19,610/-] as had been substantiated on the basis of documentary evidence by the ld. A.R, are in the nature of compensatory payments that were made by the assessee firm on account of delay in execution of the respective work orders, therefore, the same would by no means fall within the sweep of "Explanation-1" of Section 37(1) of the Act. Our aforesaid view that compensatory payments made by an assessee are duly allowable as a deduction u/s. 37(1) of the Act is supported by the judgment of the Hon'ble High Court of Gujarat in the case of Pr. CIT Vs. Mazda Ltd. (2017) 250 Taxman 510 (Guj.). It was observed by the Hon'ble High Court in its aforesaid decision that liquidated damages paid by the assessee to

customers for delay in delivery of machinery or execution of contract, i.e, at a specified percentage of value of the order, being a normal incident of assessee's business could not be said to have been incurred for a purpose which was prohibited of law and thus, was allowable as a deduction. Also, a similar view has been taken by the Hon'ble High Court of Bombay in the case of Pr. CIT Vs. Atos India (P) Ltd., ITA No.1534 of 2016. It was observed by the Hon'ble High Court in its aforesaid decision that the payment made by the assessee for delay in execution of the work could not be held to be a contingent liability and was duly allowable as a deduction. Backed by our aforesaid observations, we are of the considered view that the assessee's claim for deduction of the amount of Rs.1,09,610/- (out of Rs. 2,38,087/-) is allowable as deduction u/s.37(1) of the Act.

9. As regards the assessee's claim for deduction of the balance amount of Rs.1,28,477/- [Rs.2,38,087/- (-) Rs.1,09,610/-], we are of the considered view that the same in absence of any material on record which would go to substantiate the aforesaid claim of the assessee of having incurred/paid the same towards delay in execution

of the work order, cannot be accepted. We, thus, in terms of our aforesaid observations, direct the Assessing Officer to vacate the disallowance of the assessee's claim for deduction of the impugned penalty to the extent of Rs.1,09,610/- (supra). Thus, **Ground of appeal No.2** is partly allowed in terms of our aforesaid observations.

10. We shall now advert to the ad-hoc disallowance of the assessee's claim for deduction of traveling expenses of Rs. 81,350/-. As is discernible from record, the Assessing Officer had on an ad-hoc basis disallowed 1/4th of the assessee's claim for deduction of travelling expenses of Rs.3,25,381/- and therein, worked out a disallowance of Rs.81,350/- in the hands of the assessee. As stated by the Ld. AR, and rightly so, the aforesaid disallowance was made by the Assessing Officer merely on an ad-hoc basis in order to avoid any possible leakage of revenue. At this stage, we may herein observe, that the aforesaid disallowance made by the Assessing Officer is merely supported by general observations and not any evidence supporting the same.

11. Admittedly, an assessee's entitlement for claim of deduction of expenses u/s. 37(1) of the Act pre-supposes incurring of the expenses *"wholly and exclusively for the purpose of its business"* and as such, any expenditure which does not fall within the four corners of the statutory requirements contemplated u/s.37(1) of the Act cannot be allowed as a deduction and can justifiably be disallowed. But then, an assessee's claim for deduction of an expenditure can by no means be disallowed on an arbitrary basis and have to be supported by irrefutable observations of the Assessing Officer therein, irrefutably proving to the hilt that the assessee's claim for deduction of the expenditure does not satisfy the requirements contemplated u/s. 37(1) of the Act i.e, the expenditure had not been incurred wholly and exclusively for the purpose of business or; the expenditure is in the nature of a capital expenditure or personal expenditure of the assessee or; the expenditure incurred by the assessee was for any purpose which is an offence or prohibited by law. Now, in the case of the assessee before us, the Assessing Officer on an ad-hoc basis had disallowed the assessee's claim for deduction of certain expenses, and

the said disallowance is not supported by any material, but is merely guided by his general observations. We are unable to comprehend as to on what basis a part of the expenditure had been disallowed while for remaining has been allowed?. Apart from that, we find that there is no whisper in the body of the assessment order about any such specific expenditure which the Assessing Officer could not verify, for the reason that it was not supported by bills or vouchers. In our considered view, such ad-hoc disallowance of the assessee's claim for deduction of expenses i.e, without placing on record any supporting material can by no means be permitted. In the backdrop of the facts involved in the case before us, we find substantial force in the claim of the ld. A.R that devoid of any specific infirmity as regards the assessee's claim for deduction of the aforesaid expenditure, the ad-hoc disallowance of a part of the same in a most arbitrary and a whimsical manner by the lower authorities can by no means be held to be justified. Our aforesaid view is fortified by the order of the ITAT, Kolkata in the case of Animesh Sadhu Vs. ACIT, Circle-1, Hoogly, ITA No. 11/Kol/2013, dated 12.11.2014 and that of the ITAT, Delhi in the

case of ACIT, New Delhi Vs. M/s Modi Rubber Ltd. ITA No. 1952/Del/2014, dated 15.05.2018. Accordingly, in the totality of the facts involved in the case before us, we are unable to concur with the ad-hoc disallowance of the expenses in question by the A.O. We, thus, not finding favor with the view taken by the lower authorities set-aside the order of the CIT(A) and vacate the disallowance of Rs.81,350/- made by the A.O. The **Ground of appeal No. 1** raised by the assessee is allowed in terms of our aforesaid observations.

12. In the result, appeal of the assessee is partly allowed in terms of our aforesaid observations.

Order pronounced in open court on 30th day of March 2022.

Sd/-	Sd/-
JAMLAPPA D BATTULL	**RAVISH SOOD**
(ACCOUNTANT MEMBER)	**(JUDICIAL MEMBER)**

रायपुर/ RAIPUR ; दिनांक / Dated : 30th March, 2022
SB

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

1. अपीलार्थी / The Appellant.
2. प्रत्यर्थी / The Respondent.
3. The CIT(Appeals)-1, Raipur (C.G)
4. The Pr. CIT-1 Raipur (C.G)

5.विभागीय प्रतिनिधि, आयकर अपीलीय अधिकरण,रायपुरबेंच,
रायपुर / DR, ITAT, Raipur Bench, Raipur.

6. गार्ड फ़ाइल / Guard File.

आदेशानुसार / BY ORDER,

// True Copy //

निजी सचिव / Private Secretary
आयकर अपीलीय अधिकरण, रायपुर / ITAT, Raipur.

		Date	
1	Draft dictated on	15.03.2022	Sr.PS/PS
2	Draft placed before author	17.03.2022	Sr.PS/PS
3	Draft proposed and placed before the second Member		JM/AM
4	Draft discussed/approved by second Member		AM/JM
5	Approved draft comes to the Sr. PS/PS		Sr.PS/PS
6	Kept for pronouncement on		Sr.PS/PS
7	Date of uploading of order		Sr.PS/PS
8	File sent to Bench Clerk		Sr.PS/PS
9	Date on which the file goes to the Head Clerk		
10	Date on which file goes to the A.R		
11	Date of dispatch of order		