

**IN THE INCOME TAX APPELLATE TRIBUNAL  
"A" BENCH, AHMEDABAD**

**BEFORE SHRI T.R. SENTHIL KUMAR, JUDICIAL MEMBER &  
SHRI MAKARAND V. MAHADEOKAR, ACCOUNTANT MEMBER**

आयकर अपील सं./I.T.A. No. 666/Ahd/2024  
(निर्धारण वर्ष / Assessment Year : 2017-18)

<b>Rotomag Motors And Controls Private Limited</b> Phase IV, 2102-3, B/H. R K Metal, V.U. Nagar, Anand - 388121, Gujarat	<b>बनाम/ Vs.</b>	<b>Assistant Commissioner of Income Tax</b> Anand Circle
स्थायी लेखा सं./जीआइआर सं./PAN/GIR No. : AAACR9061K		
(Appellant)	..	(Respondent)

अपीलार्थी ओर से /Appellant by :	Shri Shailesh J. Shah, C.A.
प्रत्यर्थी की ओर से/Respondent by :	Smt. Trupti Patel, Sr. DR

<b>Date of Hearing</b>	22/08/2024
<b>Date of Pronouncement</b>	30/08/2024

**आदेश/O R D E R**

**PER MAKARAND V. MAHADEOKAR, AM:**

This appeal by the assessee is directed against the order of the Commissioner of Income Tax (Appeals) - National Faceless Appeal Centre, Delhi [hereinafter referred to as "CIT(A)"] passed u/s 250 of the Income Tax Act,1961[hereinafter referred to as "the Act"] wherein the CIT(A) upheld the disallowance of Rs. 1,14,19,990/- on account of warranty provision expenses made by the Assessing Officer (AO) as per his order passed u/s 143(3) of the Act.

### Facts of the case

2. The assessee, who is engaged in the manufacturing of engineering goods, filed its e-return for AY 2017-18, declaring a total income of Rs. 41,41,54,010/-. The case was selected for complete scrutiny under CASS, leading to the issuance of notices under Sections 143(2) and 142(1) of the Act. The core issue in the scrutiny was the assessee's claim of Rs. 1,14,19,990/- as warranty provision expenses. The provision was made in relation to a contract with the Chhattisgarh government for the supply, installation, and commissioning of solar photovoltaic (SPV) irrigation pumps, which included a five-year (60 months) on-site warranty.

3. During the course of assessment proceedings, the assessee stated that the warranty provision, amounting to 0.74% of turnover, was based on the significant scale of the project and was allowable under Section 37 of the Act. The assessee supported this claim by referencing several judicial decisions, including **Rotork Controls India P. Ltd. v. CIT (2009) 314 ITR 62 (SC)**, which established guidelines for recognizing a provision as a liability. The AO analysed the applicability of the Supreme Court's ruling in **Rotork Controls India P. Ltd. (supra)**, which laid down conditions for recognising a provision as a liability. The AO concluded that the assessee did not meet these conditions because the provision was not based on historical trends or scientific estimation, as this was the first year of operation for the SPV pumps supplied to the Chhattisgarh government and the warranty provision was deemed a contingent liability under AS-29 (Accounting Standards), as it lacked a reliable estimate based on past data. The AO further concluded that the warranty provision was an ad-hoc

estimate without a scientific basis. As a result, the provision was classified as a contingent liability by the AO and was disallowed.

4. Not satisfied with the order of AO, the assessee filed an appeal before CIT(A), who agreed with the AO's findings that the warranty provision did not satisfy the necessary criteria to be recognized as an allowable expense. As a result, the CIT(A) upheld the AO's decision to disallow the warranty provision expense of Rs. 1,14,19,990/- and add it back to the total income of the assessee.

5. Aggrieved by the order of CIT(A), the assessee is in appeal before us with following grounds of appeal:

*"1. On the facts and in the circumstances of the case and in the law the Learned Assessing officer ACIT, Anand Circle, Anand has passed the e-Assessment order in violation of principal of natural justice.*

*2. On the facts and in the circumstances of the case and in the law the Learned Commissioner of Income Tax Appeals) has erred in sustaining the addition made by the ACIT, Anand Circle, Anand treating the genuine bona fide claim of 'Provision of Warranty' of Rs. 1,14,19,990/- without appreciating that, expenses on provision for future warranty would be allowable deduction u/s.37(1) as it was not a contingent liability and that, the appellant has adduced various evidence, non-of which have been belied or disproved by the assessing officer. The said addition made by the Assessing Officer, and sustained by the Commissioner of Income Tax (Appeals) may therefore be deleted.*

*3. On the facts and in the circumstances of the case and in the Law the learned Commissioner of Income Tax Appeals) has erred in sustaining the addition made by the Assessing Officer, ignoring the fact that the appellant has produced and all every detail, documents and records proving genuineness of his impugned claim of warranty and that too without pointing out any infirmity in the details, documents and records produced by the appellant. The impugned order stating... "the relevant financial is the first year of operation for the pumps supplied by the assessee", therefore, without any*

*substance and is based on assumption and presumption. Such order cannot be sustained in the eyes of law. It may please be quashed.*

4. *That the Learned Commissioner of Income Tax (Appeals) failed to appreciate that, the sale as well as warranty are inextricably bound with each other and therefore, if the sale proceeds are taken note of in a year, the liability in respect of the warranty is also be taken note of in the same year. The liability is not contingent. It is a definite and certain liability.*
5. *That the Learned Commissioner of Income Tax (Appeals) failed to appreciate that, an assessee maintaining his account 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 business, regard being had to be accepted principles of Commercial practice an accountancy. It is not as if such deduction is permissible only in case of amounts actually expended or paid.*
6. *That the Learned Commissioner of Income Tax (Appeals) failed to appreciate that, liability to pay for warranty claims arose no sooner the sales were affected. Appellant on the basis of scientific approach for sale made during the year provision has been made. Therefore, though exact amount could not be quantified, it has to be allowed in the year of sales.*
7. *That the Learned Commissioner of Income Tax (Appeals) failed to appreciate that, if a business liability has definitely arisen in the accounting year, the deduction should be allowed although liability may have to be quantified and discharged at a future date. The liability is in presenti though it will be discharge at future date.*
8. *The appellant, therefore, submits that, the addition sustained by the Commissioner of Income Tax (Appeals) by treating the genuine and bona fide claim disallowed may be deleted and such other and further reliefs, as may be favourable to the appellant, may be granted, as may be thought fit to meet the end of justice.*
9. *The appellant craves leave to add, amend and / or alter the Grounds or Grounds of Appeal either before or at the time of hearing of the Appeal."*

### On the grounds

6. The Authorised Representative (AR) of the assessee pointed out that there was a specific condition of warranty in the Bid Document of the

Odisha Renewable Energy Development Agency which required assessee to repair and replace defective goods or part thereof, without cost to the purchaser. He further stated that this warranty was valid for 60 months after the goods or any portion thereof have been delivered and commissioned at the final destination indicated in contract. The AR submitted that the provision made for warranty expenses complied with **Accounting Standard 29 (AS-29)**, as per which -

- A present obligation existed as a result of a past event (the sale of solar pumps with a five-year warranty), creating an unavoidable obligation to settle through an outflow of resources.
- The provision was necessary due to the certainty of incurring future expenses related to warranty claims, which is consistent with the class of obligations as a whole. Therefore, the outflow of resources was expected.
- The assessee made a reliable estimate of the provision using the discounted cash flow (DCF) method. The provision was calculated at 0.74% of the turnover based on the inflow from the solar project of Rs. 136.83 crores, discounted at 14%, resulting in a provision of Rs. 1.15 crores for AY 2017-18. (Detailed working was submitted to the CIT(A))

7. The AR also contended that it has been manufacturing electric motors since 1993 and has consistently made provisions for warranty expenses in its books of accounts for several years, including for FY 2016-17. The turnover and provisions made in previous years were presented to establish the consistency and reasonableness of the provisions:

- **FY 2013-14 (AY 2014-15):** Provision of Rs. 22,00,000/- on a turnover of Rs. 25,87,35,190/-

- **FY 2014-15 (AY 2015-16):** Provision of Rs. 27,43,83,792/- on a turnover of Rs. 27,43,83,792/-
- **FY 2015-16 (AY 2016-17):** Provision of Rs. 21,50,000/- on a turnover of Rs. 92,96,45,013/-
- **FY 2016-17 (AY 2017-18):** Provision of Rs. 1,14,19,990/- on a turnover of Rs. 155,76,06,466/-

8. The AR further highlighted that for AY 2018-19 and AY 2021-22, identical questions regarding the provision for warranty expenses were raised during scrutiny, and after detailed submissions, the provisions were allowed. The amounts of provisions made and allowed were Rs. 3,98,90,990/- for AY 2018-19 and Rs. 4,68,83,555/- for AY 2021-22.

9. The AR relied on several judicial precedents to support assessee's claim that the provision for warranty expenses, even when made for the first time, is admissible if based on reasonable and scientific estimation. Notable cases cited include:

- ***CIT v. Vinite Corporation Pvt. Ltd. [2005] 278 ITR 337 (Del):*** The court allowed the provision for warranty expenses based on reasonable estimation.
- ***Rotork Controls India Ltd. v. CIT [2009] 314 ITR 62 (SC):*** Hon'ble Supreme Court allowed a provision for warranty expenses where it was based on past data and made using a reliable estimation method.
- ***Bharat Earth Movers vs. CIT [2000] 245 ITR 428 (SC):*** Hon'ble Supreme Court held that a business liability, if based on a reasonable estimate and historical data, should be allowed as a deduction even if the exact outflow occurs in a future period.

10. The AR emphasised that the warranty provision of Rs. 1,14,19,990/- made for AY 2017-18 was reversed in AY 2021-22 to the extent of Rs.

2,01,09,848/-, as the warranty period ended on 31/03/2022. The reversal was offered as income for AY 2022-23, consistent with the terms and conditions of the tender. The AR submitted copies of ledger account extracts to support the reversal of the provision.

11. The Departmental Representative (DR) relied on the order of lower authorities and did not object to the additional evidence submitted by the assessee during the course of hearing.

12. We have heard both the parties and perused the material available on records. After thoroughly reviewing the submissions made by the assessee, the compliance with relevant accounting standards, and the judicial precedents cited, we acknowledge that the provision for warranty expenses made by the assessee was grounded in a scientifically sound and consistent method. The provision was calculated using the discounted cash flow (DCF) method, which considered the inflow from the solar project, the five-year warranty period, and a discount rate of 14%. This approach provided a reliable estimate of future warranty costs, aligning with the principles established in **Rotork Controls India (P) Ltd. v. CIT (supra)** and **Bharat Earth Movers v. CIT (supra)**. The consistent use of this method across multiple years, including the subsequent assessment years (AY 2018-19 and AY 2021-22), where similar provisions were accepted by the department, further supports the legitimacy and accuracy of the assessee's approach. We find that the assessee's provision for warranty expenses complies with **Accounting Standard 29 (AS-29)**. Specifically:

- **Present Obligation as a Result of Past Events:** The provision was recognised as a liability because the assessee had a present

obligation resulting from the sale of SPV pumps with a five-year warranty. This obligation was triggered by past events (the sale and delivery of the pumps as per the terms of contract) and created an unavoidable obligation to address potential warranty claims.

- **Probability of an Outflow of Resources:** We agree with the assessee that an outflow of resources was probable, given the nature of the warranty obligations. The provision was made in anticipation of future warranty claims, which were likely given the historical data and the terms of the contract.
- **Reliable Estimate of the Obligation:** The provision was calculated based on a reliable estimation process, using a scientifically justified discount rate and consistent with industry standards. The assessee's method, which factored in both the total inflow from the project and the discounting for future liabilities, ensured that the provision reflected the best estimate of the expected warranty costs.

13. We observe that the AO allowed similar provisions in subsequent assessment years, including AY 2018-19 and AY 2021-22. This consistent tax treatment across different years indicates that the department accepted the reasonableness of the provision, further validating the assessee's approach in AY 2017-18. We also take note of the fact that the warranty provision of Rs. 1,14,19,990/- made in AY 2017-18 was reversed in AY 2021-22, and the reversal amount was offered as income in AY 2022-23. This reversal demonstrates that the provision was prudently and accurately estimated and adjusted based on actual warranty claims, further supporting its legitimacy.

14. We rely on the Hon'ble Supreme Court's decisions in **Rotork Controls India (P) Ltd. (supra)** and **Bharat Earth Movers (supra)**, which support the deduction of provisions for future liabilities when they are based on reasonable estimates and comply with recognized accounting standards. We also consider other judicial precedents cited by the assessee,

which consistently uphold the admissibility of such provisions when made on a scientifically sound and consistent basis.

15. We emphasise that provisions based on scientific methods, consistent business practices, and compliance with AS-29 should be recognized as allowable deductions. The consistent application of these principles is essential to ensuring that business liabilities are accurately reflected in the financial statements and tax assessments.

16. The disallowance of Rs. 1,14,19,990/- is directed to be deleted, and the provision for warranty expenses is allowed as a deduction under Section 37 of the Act.

17. In the result, the appeal of the assessee is allowed.

**This Order pronounced on 30/08/2024**

Sd/-  
(T.R. SENTHIL KUMAR)  
**JUDICIAL MEMBER**

Ahmedabad; Dated 30/08/2024  
S. K. SINHA

Sd/-  
(MAKARAND V. MAHADEOKAR)  
**ACCOUNTANT MEMBER**

True Copy

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

1. अपीलार्थी / The Appellant
2. प्रत्यर्थी / The Respondent.
3. संबंधित आयकर आयुक्त / Concerned CIT
4. आयकर आयुक्त(अपील) / The CIT(A)-
5. विभागीय प्रतिनिधि, आयकर अपीलीय अधिकरण, अहमदाबाद / DR, ITAT, Ahmedabad
6. गार्ड फाईल / Guard file.

आदेशानुसार/ BY ORDER,

उप/सहायक पंजीकार (Dy./Asstt. Registrar)  
आयकर अपीलीय अधिकरण, अहमदाबाद / ITAT, Ahmedabad