IN THE INCOME TAX APPELLATE TRIBUNAL, 'D' BENCH MUMBAI

BEFORE: SHRI PAWAN SINGH, JUDICIAL MEMBER
&
SHRI PRABHASH SHANKAR, ACCOUNTANT MEMBER

ITA No. 1588/MUM/2025(AY: 2017–18)
(Physical hearing)

Dai-ichi Karkaria Limited 3rd Floor, Liberty Building, Sir VT Marg, Marine Lines, Mumbai-400020.	Vs.	DCIT Circle 1(1)(1), Room No. 533, 5th Floor, Aayakar Bhawan, M.K. Road, Mumbai-400020.
PAN: AAACD0548F		
(Appellant)	..	**(Respondent)**

Assessee by	Ms. Priyanka Jain CA /AR
Revenue by	Shri. Annavaram Kosuri, Sr. DR
Date of Hearing	25/06/2025
Date of Pronouncement	30/06/2025

Order under section 254(1) of Income Tax Act

PER PAWAN SINGH, JUDICIAL MEMBER:

1. This appeal by the assessee is directed against the order of ADDL/JCIT(A), Agra dated 17.01.2025 for A.Y. 2017-18. The assessee has raised the following grounds of appeal:

" 1. On the facts and the circumstances of the case and in law, the Ld. JCIT(A) has erred in upholding the additional disallowance of Rs. 5,29,448 made by the Ld. AO under section 14A read with Rule 8D.

2. Without prejudice, on the facts and circumstances of the case and in law, the Ld. JCIT(A) erred in upholding the view taken by the Ld. AO that the Mutual Funds (Growth Option) are also covered under section 14A of the Act, without considering the fact that they did not yield any dividend income. Accordingly, the JCIT(A) should have restricted the disallowance under section 14A to Rs. 10,26,245 (as against Rs. 25,86,319 computed by the Ld. AO).

3. Without prejudice, on the facts and the circumstances of the case and in law, the JCIT(A) erred in not holding that the disallowance under Rule 8D(2)(ii) is to be computed only on investments which has earned dividends.

4. In the facts and circumstances of the case and in law, the Ld. JCIT(A) has erred in upholding the disallowance of Rs. 10,06,858 towards employee costs payable to workmen, by treating it as contingent liability.

5. On the circumstances of the case and in law, the Ld. JCIT(A) has erred in considering the 'book profits' computed at Rs. 17,41,07,134 in the computation sheet of the Assessment order, as against Rs. 17,30,91,244 computed by the Ld. AO in the Assessment order.

6. On the circumstances of the case and in law, the Ld. JCIT(A) has erred in upholding the initiation of penalty proceedings under section 270A for alleged under-reporting of income."

2. The brief facts of the case are that assessee is a company engaged in manufacturing of fertilizers and chemicals, filed its return of income for A.Y. 2017-18 on 13.10.2017 declaring income of Rs. 17.31 Crore (Cr.). The case was selected for scrutiny. During the assessment the Assessing Officer (AO) noted that assessee has shown exempt income of Rs. 6.85 Cr. The assessee made *suo-moto* disallowance under section (u/s) 14A of Rs. 20,56,871/-. The AO noted that assessee has not made disallowance as per provision of Rule 8D. The AO issued show-case notice as to why disallowance u/s. 14A should not be made as per Rule 8D. The assessee filed its reply and stated that they have already disallowed Rs. 20,56,871/- being 3.00% of exempt income of Rs. 6.85 Cr such method is being followed by assessee in earlier years and has been accepted in all earlier years. The reply of assessee was not accepted by AO. The AO recorded that the assessee has made investment in shares and mutual funds. Making investment is a decision making process which require process involving study and research. It require manpower and funds to make investment which require expenditure or cost, the cost is in the form of direct or indirect under various rate like personal cost, administration cost, interest cost etc. Contention of assessee that no direct or indirect cost was incurred in relation to earning tax

free dividend income cannot be excepted. The AO by referring the decision of Hon'ble Apex Court in Maxopp Investments (2018) 15 SCC 523/ AIRONLINE 2018 SC 1470 has noted whether dividend income has earned or not is immaterial. The AO disallowed 1.00 % of average value of investment. The total annual average was worked out by AO at Rs. 25.86 Cr. Thereby the AO worked out disallowance of Rs. 25,86,319/-. Since, the assessee already made disallowance of Rs. 20,56,871/-, thereby AO made addition of difference of Rs. 5,29,448/- and added back to the income of assessee under section 115JB in book profit.

3. The AO further noted that assessee has created a contingent liability of Rs. 10,06,858/- in its profit and loss account (P & L) on account of employees cost payable to workmen at Kasarwadi Plant. The assessee was issued show-cause notice as to why the provision of contingent liability should not be disallowed. The assessee filed its reply. In reply the assessee stated that there agreement with workers expired in November 2008, the company entered into revised wage agreements with its worker. However, certain workers did not accepted the revised wage and raised dispute/litigation which is pending before Labour Court. As per revised wage agreement, the assessee company is required to make provision of wage and accordingly same has been accrued of Rs. 10,06,858/- in the books of account for the year under consideration. Submission of assessee was not accepted by AO. The AO held that matter is pending before labour court, which itself shows that liability of the assessee company has not been fixed. The liability is unascertained liability which is contingent in nature and not allowable u/s. 37. Thereby disallowed such liability. The AO in para 6 recorded

book profit u/s. 115JB as per computation of income at Rs. 17,15,54,938/-. However, while issuing computation it stated such figure at Rs. 17,41,07,134/-. Aggrieved by the action of AO the assessee filed appeal before CIT(A).

4. Before CIT(A) the assessee filed its detailed return submission. On the disallowance of section 14A, the assessee reiterated that additional disallowance made by AO is unwarranted. The assessee made *suo-moto* disallowance of Rs. 20,56,871/- which is more than adequate and is consistent with prior years methodology. On the disallowance of employee cost in treating contingent liability, the assessee stated that provision is made on ascertained liability arising out of wage agreement with its workers and cannot be treated as contingent liability. On calculation of book profit the assessee stated that it requires rectification to correct the figure.

5. The Ld. CIT(A) on considering the submission of assessee held that the provision of section 14A read with Rule 8D are explicit in requiring disallowance of expenditure related to exempt income. The Supreme Court in Maxopp Investment Ltd. (supra) has clarified that the dominant intention behind investment is immaterial. Disallowance must be computed based on prescribed matter, if the AO is not satisfied with the computation of assessee's disallowance and upheld the action of AO. On disallowance of employees cost, the CIT(A) held that section 37 of Act permits deduction of expenses which are not contingent and are incurred wholly and exclusively for the purpose of business. In the present case, liability to pay the disputed amount depends on Labour Court decision, making it uncertain at the time of assessment. The AO reasoning is based on the decision of Supreme Court in CIT V Gemini Cashew Sales

Corporation 1967 SCR (3) 727, AIR 1967 SC-1559 wherein it was held that contingent liability depend on future events cannot be allowed as deduction. Assessee's reliance on Bharat Earth Movers V. CIT is misplaced. On the basis of such observation the Ld. CIT(A) upheld the action of AO. On incorrect computation of book profit the Ld. CIT(A) held that contention of assessee is that adjustment of section 14A and addition of contingent liability were improper and these amounts were not factual additions but imperative differences. However, as per AO's computation such computation are in align with section 115JB(2) and its explanation clauses. Thus, the adjustment made by AO is in consistent with law and biding precedent. Thereby, Ld. CIT(A) upheld the computation of book profit u/s. 115JB as well. Further aggrieved the assessee has filed present appeal before Tribunal.

6. We have heard the submission of Learned Authorised Representative (Ld. AR) of the assessee and the Learned Senior Departmental Revenue (Sr DR) for the revenue and have gone through the orders of lower authorities carefully. Ground no. 1 to 3 relates to disallowance u/s. 14A. The Ld. AR of the assessee submit that AO has not recorded any satisfaction against *suo-moto* disallowance made by the assessee and recomputed disallowance as per Rule 8D. The contention of assessee has not been rebutted by AO. The AO first required to record his satisfaction that disallowance made by assessee is not correct and then to adopt the method employed in Rule 8D. The assessee in consistently following the method in making reasonable disallowance @3.00% of exempt income which has been accepted from A.Y. 2010-2011 to 2013-14. The contention of assessee before AO as well as CIT(A) was that the investment which does not yield

dividend income is to be excluded while considering the average value of investment. In case, such investment is considered which does not yield exempt income, disallowance u/s. 14A will be restricted to Rs. 10,26,245/-, whereas the assessee has made much more *suo moto* disallowances. The AO further added the disallowance of 14A to book profit under section 115JB. To support he submissions, the Ld. AR to support his various submission relied upon the various decision in

- ACB India Ltd. v. CIT 374 ITR 108 (Delhi HC),
- Asia Investments Pvt. Ltd. v. ACIT ITA No. 5820/Mum/2015,
- J. V Holdings v. DCIT ITA No. 1337/Bang/2018,
- REI Agro Ltd. v. DCIT 160 TTJ 107 (Kolkata Tribunal),
- Air India Ltd. v. ACIT ITA No. 5632/Mum/2024,
- ACIT v. Vireet Investment Ltd. 82 taxmann.com 415 (Delhi Tribunal) (SB),
- Infina Finance Pvt. Ltd. v. ACIT 413 to 416/Mum/2024.

7. On the other hand, the Ld. DR for the revenue supported the order of lower authorities. The ld. DR submits that Hon'ble Supreme Court in Maxopp India (supra) has settled the issue. The assessee was required to make disallowance strictly in accordance with Rule 8D. So far as suo-moto disallowance by assessee @ 3% of exempt income is concerned. The ld. DR submit that such suo-moto disallowance is not in accordance with the method prescribed in Rule 8D. So far as acceptance of *suo moto* disallowances made by assessee is earlier year @ 3.00% is concerned, the ld SR DR for revenue submits that each year has to be considered separate and independent. The assessee is making disallowance in earlier years which has not been tested by any judicial authority or by revenue

authority so it cannot be claimed that suo-moto disallowance is based on such scientific method.

8. We have considered the rival submission of both the parties and have gone through the order of lower authority. There is no dispute about the quantum of exempt income. Similarly, there is no dispute about suo-moto disallowance made by assessee of Rs. 20,56,871/-. Before us, the Ld. AR of the assessee two fold submission, firstly that AO has not recorded his satisfaction about suo-moto disallowance and secondly only those investment which yield a exempt income has to be considered as per decision of special bench of Delhi Tribunal in Vireet Investment Pvt. Ltd.(supra) and Delhi High Court in ACB Ltd. V. CIT (supra). We find that no specific procedure is prescribed either in the Act or in the Rules to record the non-satisfaction on the suo moto working of disallowance of assessee under section 14A, once, the AO has not accepted the working on disallowance that itself reflects his dissatisfaction. So far as second submission of Ld. AR of the assessee is concerned, we find convincing force in her submissions that only investment which yielded exempt income is to be considered for the purpose of calculating average value of investment as per decision of special bench in ACIT V. Vireet Investment (Supra). Hence, we direct the AO is workout the figure of average value of investment as per the decision of Delhi High Court in ACB India Limited (supra) and Vireet Investment (P) Ltd (supra). The AO is further directed to follow the decision Vireet Investment (P) Ltd (supra) while computing book profit under section 115JB. Needless to direct that before passing the order, the AO shall allow reasonable opportunity to the assessee. In the result, this ground of appeal is allowed for statistical purposes.

9. Ground no. 2 relates to disallowance of employee cost payable to workers in treating it as a contingent liability. The Ld. AR of the assessee submits that assessee is a company and required to follow accounting principle while accounting income and expenditure. Section 145 of the Income Tax Act required that assessee company to follow Mercantile System of accounting which mandates accrual of all ascertained liability. During the financial year under consideration, provision was created for lowest amount as proposed in the settlement agreement with the workers which is undoubtedly payable to workers. The workers disputed the same and litigated for higher amount of wages. Thus, dispute arise between the assessee and its worker. There is dispute on excess that was demanded by workers, whereas the provision was created for ascertained liability, which was even otherwise payable if the dispute was to be decided in favour of assessee company. The assessee has already furnished working of all wages before lower authorities and copy of which is filed at page no. 193 to 195 of paper book. The disputed amount which was litigated by the workers was never provided in the books of account. The assessee company is also required to follow ICDS provision introduced in the year under consideration while computing the total income. ICDS-I relating to accounting policy mandates the assessee company to follow fundamental accounting assumption of going concern consistency and accrual of liability. The assessee has present obligation as a result of past event in case of assessee there is substantial degree of estimation thereby the liability was provided, based on settlement agreement proposed between the parties. It was reasonably setting

that there was out flow of resources with the minimum amount of liability known to the company. The dispute is only for the enhanced wages. The ratio of the decision relied by lower authorities in CIT v. Gemini Cashew Sales Corporation (Supra) in not applicable on the facts of the present case. The amount claimed by the assessee as a permissible allowance in this profit and loss account, could not be regarded as properly admissible either u/s. 10 or u/s. 10(2)(XV) of Income Tax Act 1922. Under the provision to section 25FF the liability to compensation arouse for the first time after closure of business and not before. It was not arose in carrying of the business but on account of transfer of business thus it was not a liability of revenue nature and could not be treated as permissible deduction u/s. 10(1) of old Income Tax Act. Thus, the facts of said case are aquarians.

- Bharat Earth Movers V. CIT (2000) 112 taxman 61 (SC),
- Rotork Controls India (P.) Ltd. v. CIT (2009) 108 taxman 422 (SC),
- CIT v. Kerala State Financial Enterprises Ltd. (2009)178 taxman 449 (Kar.) (HC),
- Housing & Urban Development Corporation Ltd. v. ACIT (2020) 115 taxmann.com 166 (Delhi) (HC),
- CIT V. Indian Metal and Metallurgical Corporation (1964)51 ITR 240 (Mad.) (HC),
- CIT v. Premier Vegetable Products (1997) 227 ITR 931 (Raj.) (HC),
- CIT v. United Motors (India) Ltd. (1990) 181 ITR 347 (Bom.) (HC),
- Indian Express Newspaper Ltd. v. FCIT (2024) 298 taxman 507 (Bom.) (HC),
- Mahindra & Mahindra Ltd. v. ACIT ITA No. 1448/Mum/2016,
- CIT v. Bharat Heavy Electrical - Limited IT Appeal NOS. 278, 312, 807 - And 1578 OF 2010 (Delhi) (HC).

10. On the other hand, the Ld. DR for the revenue supported the order of lower authorities. The ld. DR for the revenue submits that liability has not been

crystalised. The liability is a contingent liability which is not permissible. There is no certain degree of amount.

11. We have considered the rival submissions of both the parties and have gone through the order of lower authority. There is no dispute that assessee has created a provision of workers payment on account of wage revision. The lower authorities stated this as contingent and as unascertained liability. We find that Hon'ble Delhi High Court in a recent decision in Housing & Urban Development Corporation Ltd. V. ACIT [2020] 421 ITR 599 (Delhi) held that provision made by assessee Public Sector unit for revision of pay of its employees, as per recommendation of committee appointed by the government was to be allowed as a business expenditure. Assessee has made provision on the basis of pending demand of workers on account of revision labour payment. Thus, assessee is eligible for allowance of such expenditure. In the result, ground no. 4 of the assessee is allowed.

12. Ground no. 5 relates to book profit roundly computed in computation sheet. Considering the fact that there is mismatch in the book profit computed in assessment order and shown in the computation sheet. The AO is directed to verify the fact and correct the figure of book profit accordingly.

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

Order pronounced in open court on 30.06.2025.

Sd/-	**Sd/-**
(PRABHASH SHANKAR)	**(PAWAN SINGH)**
ACCOUNTANT MEMBER	**JUDICIAL MEMBER**

Mumbai; Dated 30/06/2025
Anandi Nambi, *Steno*

Copy of the Order forwarded to:

1. The Appellant
2. The Respondent.
3. CIT
4. DR, ITAT, Mumbai
5. Guard file.

BY ORDER,

(Asstt. Registrar)
ITAT, Mumbai