(2007) 09 DEL CK 0039

In the Delhi High Court

Case No : ITR No. 153 of 1986

R.C. Gupta APPELLANT

Vs

Commissioner of Income Tax RESPONDENT

Date of Decision : 03-09-2007

Acts Referred:
Income Tax Act, 1961 — Section 41(1)

Citation : (2008) 218 CTR 315 : (2008) 298 ITR 161 : (2008) 166 TAXMAN 191

Hon'ble Judges : Madan B. Lokur, J;Dr. S. Muralidhar, J

Bench : Division Bench

Advocate : Rajiv Saxena, for the Appellant; Sanjeev Sabharwal, for the Respondent

Judgement

S. Muralidhar, J.—Relevant to the Assessment Year 1979-80 following question has been referred for our opinion:

Whether, on the facts and in the circumstances of the case, the Income Tax Appellate Tribunal was justified in law in holding that the disputed liability of Rs.50,761 was not allowable as deduction in the Assessment Year 1979-80?

2. On a scrutiny of the assessed''s Trading Account the Assessing Officer (''AO'') noticed that during the Assessment Year 1979-80 a sum of Rs.50,761 stood debited to the raw material account. The Explanation of the assessed was that this amount was payable to M/s. Hindustan Steel Limited for certain purchases which had been made on 22.10.1975 but in respect of which the assessed had disputed its liability. According tot he assessed the liability stood accrued in the financial year ending 31.3.1979 since a suit for recovery had been filed by Hindustan Steel Limited against it on 18.8.1978. The Assessing Officer disallowed the claim on the ground that the said amount did not relate to any purchases made during the previous year 1978-79 relevant to the Assessment Year 1979-80. The appeal filed by the assessed was allowed by the Commissioner of Income Tax (Appeals) [''CIT (A)'']. Relying on the judgment of the Hon''ble Supreme Court in The Kedarnath Jute Mfg. Co. Ltd. Vs. The Commissioner of

Income Tax, (Central), Calcutta, , the CIT (A) held that the liability of Rs.50,761 had accrued against the assessed during the accounting year ending on 31.3.1979.

3. The Revenue''s appeal to the Income Tax Appellate Tribunal (''Tribunal'') was allowed. According to the Tribunal, the liability in question "would accrue or arise only when either the Court decree is made against the assessed or when the matter is amicably settled between the assessed and the Hindustan Steel Limited." Referring to the decision of the Allahabad High Court in Swadeshi Cotton Mill Co. Ltd. Vs. Commissioner of Income Tax, , the Tribunal held that that as long as the dispute continued and the assessed kept resisting liability, it would not be entitled to claim the deduction even if it followed the mercantile system of accounting.

4. Learned Counsel for the assessed contended that the liability accrued to the assessed the minute purchases were made. Merely because the assessed had disputed the liability did not mean that it ceased to be a liability. He submitted that once a suit was filed for recovery of the said sum by Hindustan Steel Limited, the liability became an ascertained one. Since the assessed followed the mercantile system of accounting it was bound to account for the said liability by making a provision therefore. In any event if at a subsequent point in time the suit was dismissed, the Petitioner would be required to offer the said amount to tax in terms of Section 41(1) of the Income Tax Act, 1961.

5. Appearing for the Revenue, Mr. Sanjeev Sabharwal, learned senior Standing Counsel, submitted that the liability in instant case was contractual and not an ascertained liability. As held by the Tribunal, the criteria for determining the nature of a statutory liability, as explained in Kedarnath Jute Manufacturing Company Limited, could not be applied to the instant case.

6. In Kedarnath Jute Manufacturing Company Limited the Hon''ble Supreme Court was dealing with the case where the assessed company, which followed the mercantile system of accounting, claimed a deduction on account of sales tax for the sales made by it during the calendar year 1954 relevant to the Assessment Year was 1955-56. The assessed contested the liability and the Assessing Officer rejected its claim on that ground. The deduction was also disallowed on the ground that the assessed had not made any provision in its books for the payment of sales tax. The Hon''ble Supreme Court held that the liability did not cease to be a liability only because the assessed had contested the liability by initiating proceedings for getting it reduced or wiped out.

7. In J.K. Synthetics Ltd. Vs. O.S. Bajpai, Income Tax Officer, Central and Another, the Allahabad High Court held that an assessed following the mercantile system could legitimately claim a deduction in respect of a business liability, which in that case was excise duty, even where such liability had not been quantified or paid or was disputed. This decision was upheld by the Hon''ble Supreme Court in Union of India and another Vs. M/s. J.K. Synthetics Ltd., . In

Swadeshi Cotton Mill Co. Ltd. the Allahabad High Court was dealing with the case involving a non-statutory disability. There the assessed had claimed deduction of Rs. 18,533 being a sum paid to the Ahmedabad Textile Industry Research Association towards its annual contribution for the year ending 31.3.1958. There was a dispute about a bill raised by the Association and the payment was ultimately made by the assessed only in the previous year relevant to the Assessment Year 1960-61. Although the liability was not a statutory one, it was held that the said liability, relatable to the period 1.4.1957 to 31.3.1958, had accrued only in the previous year relevant to the Assessment Year 1960-61 and hence should be allowed in that year.

8. The Hon''ble Supreme Court in Bharat Earth Movers Vs. Commissioner of Income Tax, Karnataka, reiterated the principles for deciding whether a business liability is an ascertained or a contingent one. The Hon''ble Supreme Court held (p. 431-432):

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.

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 assessed maintaining his accounts on the 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 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 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.

9. The liability in the instant case was capable on being estimated with reasonable certainty when a recovery suit was filed by Hindustan Steel Limited against the assessed on 18.8.1978. Merely because the liability was not a statutory one it could not be said that the liability that was not an ascertained one but a contingent one.

10. In view of the settled law and in the facts of the present case, we are of the view that the claim of the assessed for deduction of Rs.50,761 towards disputed liability should be allowed in the Assessment Year 1979-80.

11. Accordingly the question referred for our opinion is answered in the negative that is in favor of the assessed and against the Revenue. The reference stands disposed of.

