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* **IN THE HIGH COURT OF DELHI AT NEW DELHI**

\+ **ITA 324/2005**

Date of decision: 12th December, 2017

COMMISSIONER OF INCOME TAX, DELHI ..... Appellant
Through Mr. Ruchir Bhatia, Advocate.

versus

NARINDERJIT SINGH .... Respondent
Through Ms. Bhakti Pasrija Sethi, Advocate.

CORAM:
HON'BLE MR. JUSTICE SANJIV KHANNA
HON'BLE MS. JUSTICE PRATHIBA M. SINGH

SANJIV KHANNA, J. (ORAL)

The present appeal by the Revenue in the case of Narinderjit Singh relates to assessment year 1997-98 and arises from the order of the Income Tax Appellate Tribunal dated 15th September, 2004 in ITA No. 4577/DEL/2000.

2. The appeal was admitted for hearing vide order dated 9th November, 2006 on the following substantial question of law:-

> "Whether the amount of Rs.62,99,100/- being the provision made by the assessee on account of claim by the principal contractor due to deficiency in contract work is a contingent liability or an ascertained liability so as to entitle the assessee to claim deduction?"

3. The respondent-assessee is a proprietor of M/s. N.J. Design Build, who were assigned work as sub-contractor by M/s. Bhasin Associates (P) Limited (*BAPL, for short*) in November, 1991 to execute unfinished part of the contract for construction of influent pumping station at Ghatkopar for the Municipal Corporation of Greater Bombay, Maharashtra (*BMC, for short*). As per the agreement between the respondent-assessee and BAPL, the entire amount receivable by the latter on account of the aforesaid project was to be transferred to the respondent-assessee as consideration.

4. The respondent-assessee had started the aforesaid construction in the previous year relevant to the Assessment Year (*'AY', for short*) 1992-93 and the contract was completed in the previous year relevant to the AY under consideration i.e. 1997-98. The respondent-assessee had for the purpose of taxation opted for 'completed contract method'.

5. Return of income filed by the respondent-assessee on 27th October, 1997, declaring loss of Rs. 4,18,980/-, was taken up for scrutiny assessment. The assessment order dated 24th March, 2000 records that, pursuant to the directions issued under Section 144A of the Income Tax Act, 1961 (*Act, for short*), the income of the assessee for earlier AYs 1992-93 to 1996-97 was brought to tax by applying "percentage completion method" @ 12% of gross receipts. Administrative expenses were allowed therefrom. On this basis, the Assessing Officer (*'AO', for short*) computed the net business income of the assessee for the assessment year 1997-98 at loss of Rs.3,48,842/-. However, he made an addition of Rs.62,99,100/-, which had been claimed as business expenditure by the assessee, on the ground that it was a contingent liability which had not arisen and, therefore, was not ascertained or accrued

liability allowable as an expenditure. The aforesaid amount had been claimed by BMC from BAPL against rectification and balance work not completed. BMC has filed an arbitration suit against BAPL for recovery of Rs.54.10 crores and also put forward a claim of Rs.5,00,000/- on account of legal expenses. He observed that Rs.62.99 lacs, which had been claimed as liability by the respondent-assessee constituted a part of the demand of Rs.54.10 crores raised by BMC against BAPL in the arbitration proceedings. Accordingly, the respondent-assessee had accepted liability of Rs.62.99 lacs and, hence, the respondent's claim that Rs.62.99 lacs was actual liability was rejected, observing that it was self-contradictory. Referring to the stand taken by the respondent-assessee, the assessment order also records that the assessee was not clear whether he was disputing the demand of Rs.62.99 lacs.

6. Against the disallowance of Rs.62.99 lacs as expenditure, the respondent-assessee preferred an appeal, which was allowed by the Commissioner of Income Tax (Appeals), who referred to the agreement between the respondent-assessee and BAPL, copy of the claim made by BAPL on the respondent-assessee vide letter dated 23rd September, 1996, copy of the agreement between the respondent-assessee and BAPL on the defect liability period, imperfections and rectifications. The said order also refers to several other letters exchanged between the respondent-assessee and BAPL, and BMC and BAPL. In particular, reference was made to letter dated 20th November, 1996 along with enclosures written by BAPL acknowledging confirmation of the claim of Rs.62 crores in their favour by respondent-assessee vide earlier letter dated 15th October, 1996. He observed that the respondent-assessee had admitted his liability in these

letters to BAPL, who was the principal contractor. The letters affirmed that the respondent-assessee had accepted liability having failed to fulfil his commitment to BAPL. The observations made by the Commissioner of Income Tax (Appeals) in this regard read as under:-

> "I have carefully considered the arguments of the A.O. and the submission of the appellant. The A.O. has discussed at length the inadmissibility of the claim for Rs.54.1 crores. The issue of the allowance of this claim is not in appeal expect for an amount of Rs. 62,99,100/- which was separately claimed by the appellant. The A.O. made disallowance of Rs.54.1 crores and Rs.62,99,100/-in the same breath. The arguments given by her for disallowing the claim of Rs.54.1 crores was applied in relation to the claim of Rs.62,99,100/-also. However a distinction needs to have been made for appreciating both the claims. The bigger claim was rightly refused because it had neither been accepted by the appellant not had been ascertained or quantified.
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> But the situation with regard to the claim of Rs.62,99,100/- is different as there is no dispute about the pending work. In fact the quantification by the BMC for this work as per final claim made by it is yet higher at about Rs.1.36 crores. The A.O. has given reason for not accepting the claim of the assessee in Para 29 of the assessment order on the basis of the finding given in Paras 15-18 of the assessment order by holding that since the assessee has neither rectified the pending work not has made the payment so far to BMC or any other contractor for the liability admitted by him the same cannot be allowed. In

her opinion the admission of liability should be supported by an action of actual payment or rectification of the defective work though it has been admitted by the A.O. that the BMC has got pending/ rectification work done through other parties. She has also stated that since the assessee is disputing the liability of Rs.54.10 crores and the amount of Rs.62,99,100/- also forms part of the same the quantification of this liability has not been correctly worked out. In her opinion if the assessee decides to complete the work he may spend more or less money. Therefore, in her opinion this was a contingent liability and was not an allowable deduction. A contingent liability is certainly not admissible under the Income-tax law even if the assessee is following mercantile system of accounting. But the nature of the contingent liability is that it is not actually an existing liability of the time but is in the nature of putting aside of money which may become existent on the happening of an event. In this case the liability calculated by the appellant did not depend upon any future event. The claim was made by the BMC for deficiency in the contract work undertaken by the appellant. The main contractor had passed on this liability to the appellant who was covered by same terms of agreement as the main contractor and the appellant had accepted this liability. No future event was involved in this process. The courts have held that difficulty in ascertaining the quantum of liability does not prevent the accrual of liability. If the estimate is wrong the taxing authority would be competent to substitute his own estimate ignoring the estimate of the

> assessee but this fact alone would not mean that the liability had not accrued. This was so laid down by the Hon'ble Supreme Court in the case of Calcutta Co. Ltd. Vs. CIT 37 ITR Page-1. The High Court of Kerala in CIT Vs. Kerala Transportation Co. has also held that for considering the question of legal liability in a mercantile system of accounting only concern can be that of legal liability arising in relevant assessment year and fact that liability has not been quantified for payment which law enjoins upon assessee to cannot be relevant (2000) 111 Taxman 612). An enforceable liability against the assessee was created in the year through the principal contractor by the BMC. This liability was not only quantified in the year but was also accepted by the assessee in the year. Assessee has been following mercantile system of accounting and the project in which the liability was created came to an end in this year. Therefore the claim could only have been ascertained and made in this year. Under the circumstance and in view of decisions mentioned supra, the deduction of Rs.62,99,100/- is allowable. If subsequently there is a remission of liability, such remission would attract provisions of Section 41(1) of the Act. The A.O. is directed to allow the same."

7. Aggrieved, the Revenue preferred further appeal which has been dismissed by the impugned order dated 15th September, 2004, passed by the Income Tax Appellate Tribunal. The impugned order after referring to the order passed by the AO and the first appellate authority held that the assessee had accepted the liability and, therefore, the same was not contingent. There being no dispute between the assessee and BAPL, the

liability or expenditure was to be allowed as a deduction under the year in consideration.

8. We had asked and called upon the counsel for the appellant-Revenue to ascertain the fate of the arbitration proceedings and whether the amount of Rs. 62.99 lacs was brought to tax in any year. Counsel for the Revenue has ascertained and stated that the amount of Rs. 62.99 was brought to tax in the assessment year 2002-03 pursuant to the return filed by the assessee himself including this amount in the taxable income for the said year and under the head "other income".

9. We would have examined and gone into the question whether the aforesaid amount of Rs.62.99 lacs was contingent or actual liability in some detail, but find ourselves handicapped as the appellant-Revenue has not placed on record a copy of the agreement between the respondent-assessee and BAPL as also correspondence extensively referred to by the Commissioner of Income Tax (Appeals). We may, in this connection, produce the relevant portions of the order of the first appellate authority regarding and dealing with the said aspect:-

> "Before me learned counsel for the appellant appeared and filed written submission alongwith paper book. It is stated that the A.O. has given a finding by not properly appreciating the facts in entrity (sic). He stated that it is not the appellant who has contested the claim of the BMC but it is the principal contractor Bhasin Associates (P) Ltd. In support of the facts, the appellant filed the following documents and stated that the same were filed before the A.O. also.

A. Copy of the agreement of the appellant with Bhasin Associates (P) Ltd or BAPL

B. Copy of the claim made by BMC on BAPL

C. Copy of the claim lodged by BAPL on the appellant vide letter dated 23.9.96.

D. Copy of the clauses for defect liability period and liability for defects and imperfections and rectification thereof.

E. A photocopy of the letter dated 28.02.2000 alongwith its encloses.

F. Photocopies of the letters dated 03.08.1995, 29.09.1995 and 29.08.1996 written by BMC about pending work.

G. A copy of justification note filed before the A.O. with the letter dated 27.01.2000

H. Copies of the Notification u/s 154(2) of the Act bearing No. S069 (E) and the notification No. 994 (F. No. 132/7/95-TPL) both dated 25.01.1996 about method of accounting and estimated provision of expenses to be incurred against the work already completed.

I. A copy of the letter dated 29.09.1995 of BMC to BAPL alongwith enclosures.

J. A copy of the letter dated 20.11.1996 alongwith enclosures written by BAPL acknowledgement of confirmation of claim of Rs. 62 lakhs in their favour by the appellant vide letter dated 15.10.1996.

K. A specific confirmation from Bhasin Associates Ltd. Certifying admitted claim of Rs. 62,99,100/- by

the appellant in its favour in respect of BMC, Ghatkoper, Mumbai Project.

L. A letter from the appellant to the said effect giving categorical confirmation vide letter dated 15.10.1006.

It was submitted that there was no dispute between the appellant and BAPL the principal contractor. The appellant admitted his liability to that extent as he failed to fulfil (sic) his commitment to complete the work and as happens in every government contract the governments is empowered to get the uncompleted work finished from other sources at the risk and cost of the earlier contractor. Such amount can be recovered thereafter by the Govt. from the contractor as land revenue. It is pointed out by the learned counsel that as per Para 48 and 49 of the claim filed by BMC against the main contractor BAPL had failed to execute the said work and the said work resulted into additional liability of Rs.20.91 lakhs the calculation of which has been given in exhibits EE-1 and EE-2 attached thereto. Similarly in exhibit 33 forming part of Para 57 of the claim it has been shown that benching concrete work was got done by BMC as the main contractor failed resulting into an additional cost of Rs.116 lakhs. Para 60 of the claim document also shows in exhibit LL the additional cost of RS. 9.18 lakhs paid by BMC because of failure of BAPL Para 73 of the claim filed by BMC shows that it had incurred an expenditure of Rs.1 crore for the repairs and servicing of machines and equipment at the site due to failure of the contractor. The working of this amount is given on page 82 of the claim. All these factors go to prove that the contention of the assessing officer that the appellant failed to substantiate that the

work had already been completed by alternate contractors is incorrect. Can it be stated that the BMC (a government body) made false claims. It is stated that in view of the said facts the other contention of the A.O. that the liability was contingent also becomes baseless.

Further it was stated that in terms of clause No. 3 of the agreement dated 1.11.91 between the appellant and the main contractor all future liabilities were to be borne by the appellant to the entire exclusion of the main contractor and therefore the same was accordingly provided in the books of account. My attention was also drawn to clause No. 76 of the Arbitration claim of the BMC which clearly stipulates the working of claim of Rs.54.1 crores against the main contractor. This included not only erection of new work but also expenses of Rs.1 crore incurred on repairs and servicing of the machinery equipment at site. This is specifically mentioned in Para 73 of the claim. The total computation of claim is given in exhibit YY of the claim as per enclosed photocopy of the same. The amount determined as payable by the appellant to the main contractor includes the cost of rectification as well as balance work. It is stated that the claim of Rs. 54.1 crores contains interest claimed at Rs.52.18 crores besides Rs.56.4 lakhs for illegal occupation of land. It these two figures are excluded from the total claim, then the actual claim of the BMC remains Rs. 1.36 crores only against which the appellant has admitted a liability of Rs.62.99 lakhs. A reconciliation of the pending work

claimed by the BMC and quantified by the appellant at Rs.62.99 lakhs has also been filed.

In respect of the issue alleged by the A.O. that certain amounts included in the claim of RS.54.1 crores made by the BMC are also included in the admitted liability of Rs.62.99 lakhs of the assessee, it was stated that the same is correct.

A copy of the letter dated 29.08.96 issued by BMC attaching therewith the list of pending balance and rectification work has been filed. Since the said work was factually incomplete and pending the appellant conceded the same and valued its cost at Rs.62.99 lakhs. The items mentioned in the said list to BMC tally item by item in the Valuation made by the appellant and the main contractor as per details given on pages 52 & 53 of the paper book filed earlier. Further, it is stated that from exhibits RR and YY which form part of the claim of the BMC, it would be seen that for the rectification items claim was for Rs.14.10 lakhs as against which the assessee admitted a liability of Rs.8,79,600/-as per details given on page 52 of the paper book. Similarly the first item in the exhibit YY claimed at Rs. 20.94 lakhs has been admitted by the asses-see at Rs.20 lakhs as item 9a as per details given on page 53 of the paper book. The second item in the exhibit YY claimed at Rs.1.15 lacs has been admitted at Rs.1 lakh by the assessee in the said list. For the balance item the BMC made a claim of Rs.1 crore in lump sum as per item 5 of the exhibit YY and in which SI. No 4 is the claim for Rs.14.10 lakhs. The item No.3 of the exhibit YY is for miscellaneous work got done as per exhibit LL which are also

part of balance work as per page 53 of the paper book.

The learned counsel also stated that since the claim was made by the BMC for pending/ rectification work, the appellant conceded the same as per its own cost whereas the cost estimated and claim made for the same by BMC was of much higher amount. Thus the same items have to form part of both the figures. He fairly conceded that factually inadvertent error occurred when the claim was made for Rs.54.1 crores whereas the same should have been for an amount lower by Rs.62.99 lakhs and at Rs.53.47 crores. The A.O. has discussed the same in context of the claim for Rs.54.1 crores, an issue which is not pending in this appeal as no ground for the same has been taken in this appeal.

Finally it was stated that claim of BMC is for a bigger amount yet the assessee has admitted his liability unconditionally to the extent of Rs.62.99 lakhs only vide letter dated 15.10.99 and the said confirmation was accepted by the main contractor on 20.11.96 as per its letter of the said date. Thus the liability arose during the period under consideration only. The appellant is not liable to make any payment to BMC. His liability is limited to the main contractor only for whom he was working and if the main contractor is raising disputes with the contractor party then it does not mean that the liability of the appellant as sub-contractor is also disputed. In case the main contractor gets some concessions from the contractee then it may be the income of the main contractor of if the same is passed on the sub-contractor then it shall become income of the sub-contractor u/s 41 (1) of the Act for the year, when it will be remitted by way of concession.

> For such eventualities only, this section has been introduced in the Statute. Any subsequent probable remission cannot influence the result of an earlier year if as on the closing date of the earlier year, the nature of subsequent event was not know. Further the counsel for the appellant has place reliance on certain decisions. On the basis of the above arguments the learned counsel prayed that the action of the A.O. in rejecting the deduction of Rs.62,99,100/-should be reversed."

10. In the absence of the said documents and papers, it would be hazardous and difficult for us to answer the question framed above without examining the contents of the agreement and correspondence exchanged between the parties. Noticeably, the exchange of correspondence itself between the respondent-assessee and BAPL, and BAPL and BMC remained undisputed and was not under challenge.

11. In view of the aforesaid position, we decline and do not answer the question of law as the appellant-Revenue has not placed on record the said letters including the agreements mentioned above. Without the said documents, it will not be possible to answer the question. The case of the respondent-assessee as accepted by the first appellate authority and the Tribunal is that they had accepted and admitted their liability to pay Rs. 62.99 lacs to BAPL. That facet cannot, in absence of documents, be rejected and upset by us without the said documents on record. Accordingly, we decline to answer the question of law raised by the appellant-Revenue in the absence of documents and papers on record. There

would be no order as to costs.

SANJIV KHANNA, J.

PRATHIBA M. SINGH, J.

DECEMBER 12, 2017
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