IN THE HIGH COURT OF GUJARAT AT AHMEDABAD

TAX APPEAL No. 379 of 1999

For Approval and Signature:

HONOURABLE MR.JUSTICE D.A.MEHTA Sd/-

HONOURABLE MR.JUSTICE S.R.BRAHMBHATT Sd/-

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1 Whether Reporters of Local Papers may be allowed to see the judgment ? NO

2 To be referred to the Reporter or not ? NO

3 Whether their Lordships wish to see the fair copy of the judgment ? NO

4 Whether this case involves a substantial question of law as to the interpretation of the constitution of India, 1950 or any order made thereunder ? NO

5 Whether it is to be circulated to the civil judge ? NO

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M/S. NAVJIVAN ROLLER FLOUR & PULSE MILLS LIMITED. - Appellant(s)

Versus

THE DEPUTY CIT (ASSTT) - Opponent(s)

========== **Appearance :**
MR JP SHAH for Appellant(s) : 1,
MR KM PARIKH for Opponent(s) : 1,
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CORAM : HONOURABLE MR.JUSTICE D.A.MEHTA

and

HONOURABLE MR.JUSTICE S.R.BRAHMBHATT

Date : 04/03/2009

ORAL JUDGMENT

(Per : HONOURABLE MR.JUSTICE D.A.MEHTA)

1. On 06.09.2000 the Appeal came to be admitted by formulating the following substantial question of law:

> *"Whether the liability of Rs.7,14,824/- arising under the arbitration award against the appellant declared in the assessment year 1988-89 and not accrued in that year only because the award was challenged in appeal by the assessee and therefore was not allowable in the assessment year 1988-89?"*

2. The Assessment Year in question is 1988-8

9, the relevant accounting period being year ended on 30.09.1987. Originally assessment was framed vide order dated 01.10.1990 made under section 143(3) of the Income Tax Act, 1961 (the Act). Subsequently by an order made under section 263 of the Act, Commissioner of Income Tax, Baroda, set aside the assessment order holding that the same was erroneous and prejudicial to the interest of the revenue on the ground that the Assessing Officer had wrongly allowed deduction of Rs.7,14,824/- on account of damages on the basis of arbitration award dated 28.05.1987 which had been challenged by the assessee. The Assessing Officer thereupon framed fresh assessment under section 143(3) read with Section 263 of the Act on 22.03.1995 disallowing the amount of damages to the tune of Rs.7,14,824/-. The assessee carried the matter in Appeal and succeeded before Commissioner (Appeals). Revenue preferred Second

Appeal before the Tribunal and vide impugned order dated 20.05.1999 Revenue's Appeal came to be allowed by the Tribunal holding that no liability had been incurred by the assessee in the period relevant to the Assessment Year in question.

3. The learned Counsel appearing for the Appellant submitted that the Tribunal had failed to appreciate the fact that the assessee was following mercantile system of accounting. That accordingly on the day an Award came to be made, viz. 28.05.1987, where under the assessee was called upon to pay damages of US$ 51,329/- (on conversion amounting to Rs.7,14,824/-), the assessee had incurred liability and was entitled to claim deduction thereof. In support of the submission made reliance was placed on judgment of this Court rendered in case of *CIT Vs. Official Liquidator, Ahmedabad Manufacturing And Calico Printing Co. Ltd. (2000) 244 ITR 156* as well as judgment of Allahabad High Court in case of CIT Vs. Sugar Dealers (1975) 100 ITR 424, to submit that merely because the Award was disputed in an Appellate Forum it could not be stated that the liability to make payment had not been incurred.

4. On behalf of the respondent authority the learned Counsel submitted that though the Award was made on 28.05.1987 the same had not attained finality as the assessee had filed an Appeal which came to be decided only on 22.3.1989 and hence, the liability to make payment can be said to have been incurred only in Assessment Year 1989-90. It was submitted that this was not a case of statutory liability but a contractual liability and hence, unless and until it was finally settled, there was no question of allowing such deduction.

5. The basic facts as noted by the Tribunal are :

> *2... The assessee company is engaged in the business of manufacturing dal, besan, maida, sooji etc. The assessment year involved in both the appeals before us is 1988-89 for which the previous year ended on 30.9.87. The assessee had entered into a contract with M/s. J. K. International Pvt. Ltd., Australia based company for import of 1575 metric tones of yellow gram at the rate of 310 US dollars per metric tonne from Australia. As per the terms of the contract, the assessee was required to open an irrevocable letter of credit with an Indian Bank on or before 14.8.1986. This date was subsequently extended to 1.10.86 by the Australian party. The assessee however, failed to open the letter of credit even by the extended date and in fact repudiated the contract through their letter dated 29.8.86 to the brokers M/s. Vaidehi Spices Agency, Bombay. Arbitration proceedings were initiated by the Australian party before the Grain and Feed Trade Association (GAFTA). However, the assessee objected to the jurisdiction of GAFTA and claimed that no written agreement exist with the Australian party and there was no occasion to refer any dispute between the parties to Arbitration within GAFTA and that GAFTA have no competence or jurisdiction to proceed to make any award or decision in the matter. The assessee further submitted that the failure to open the letter of credit due to the fact that the brokers failed to furnish copies of credit notes duly signed by the Australian party. GAFTA however passed the award of Arbitration on 28.5.87 where under the assessee was to pay damages of US Dollars 51329 representing the differences between the contract price of US Dollars 310 per metric tonne and market rate of the goods on the date of default being US Dollars 277.41. Further interest was also to be paid at the rate of 9.2% per annum from*

29.8.1986 (date of default) to 28.5.87 (date of the award).The assessee did not accept the award of arbitration and the Board of Appeal under the GAFTA decided the matter against the assessee.

6. It is not in dispute that the Revenue does not dispute incurring of liability in principle. The dispute is primarily as to in which year has the liability been incurred by the assessee : the assessee claiming it to be in the year under consideration, whereas the Revenue claiming the same to be in Assessment Year 1989-90.

7. The Tribunal has categorically found that on the basis of material available on record, it was clear that the contract did not provide for payment of any particular amount as damages in case of breach of contract and the claim by the Australian party was for unliquidated damages. Therefore, it is not possible to accept the contention that the liability is contractual in nature, viz. one which has arisen on the basis of the terms of the contract.

8. In mercantile system of accounting it is well settled that both receipt and liability accrue at the earliest point of time and are not postponed merely on the basis of an entry made or absence of an entry. ***Admittedly, the assessee is following mercantile system of accounting. On 28.5.1987 when the Trade Association made an Award for damages for breach of contract the liability to pay such damages had already been incurred by the assessee. Merely because***

the Award was challenged in Appeal by the assessee cannot be a ground for holding that the liability had not been incurred. The Tribunal has committed an error in law in placing reliance upon the decision relatable to a claim for enhancement of compensation in land acquisition case and applying analogy thereof for coming to the conclusion that the liability arose only on 22.3.1999, when the Appellate Forum confirmed the Award. The issue before the Tribunal was not in relation to any claim for enhancement in the Award nor was the assessee claiming any amount over and above the awarded amount.

9. In the case of *CIT Vs. Official Liquidator, Ahmedabad Manufacturing And Calico Printing Co. Ltd.(supra)* in almost similar fact situation this Court has held that the liability to make payment of salaries and wages under the Award of the Industrial Tribunal had arisen and the Award not having been stayed became operative and/or enforceable for the relevant Assessment Year. Therefore, the liability arose in the hands of the assessee and merely because the Award was challenged that fact did not make the Award unenforceable at law. The assessee was accordingly held entitled to claim deduction in the said case.

10. In the result, for the reasons aforestated, it is not possible to hold that the impugned order of Tribunal is correct in law. The liability to make payment of Rs. 7,14,824/- arising under the Arbitration Award declared in the relevant accounting period for Assessment Year 1988-89 had

accrued in that year. The question stands answered accordingly i.e. in favour of the assessee and against the Revenue.

11. The Appeal is allowed accordingly with no order as to costs.

Sd/- Sd/-
(D.A.Mehta, J.) (S.R.Brahmbhatt, J.)