

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

+ **ITA No.1774/2010**

Date of Decision :10.08.2011

RAMPUR ENGINEERING CO. LTD. Appellant

Through: Mr. Suresh Ramchandani, Advocate for
the appellant.

Versus

**COMMISSIONER OF INCOME-TAX, NEW DELHI
... Respondent**

Through: Mr. Abhishek Maratha, Sr. Standing
Counsel for the respondent with Ms
Teena Sharma, Advocate.

**CORAM:
HON'BLE MR. JUSTICE A.K. SIKRI
HON'BLE MR. JUSTICE M.L. MEHTA**

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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 the judgment should be reported in the Digest ? | No |

A.K.SIKRI, J. (Oral)

1. Admit. Following substantial question of law arises for consideration:

"Whether on facts and circumstances of the case, the Ld. Tribunal was justified in holding that a liability otherwise accrued and deductible under the Act becomes a contingent liability only because a consent of the Board or the Appellate Authority is required for its recovery under the provisions of Section 22 and Section 22-A of the Sick Industrial Companies (Special Provisions) Act, 1985?"

2. We have also heard the arguments of counsel for both the parties finally and proceed to decide the above said question.

3. The appellant/assessee is engaged in the business of manufacture of material handling equipments like Belt Conveyer, Chain Conveyers, Idlers, Pulleys etc. This company was incorporated in the year 1943. However, sometime in the early nineties the assessee ran in the rough weather and its financial network eroded. Under these circumstances as per the Provisions of Sick Industrial Companies (Special Provisions) Act, 1985, it approached The Board for Industrial and Financial Reconstruction ('BIFR' for short) for reconstruction/rehabilitation. A reference was registered and Operating Agency (OA) was appointed to formulate a rehabilitation scheme. After the scheme was formulated, it was put up before BIFR on 01.05.1995. The scheme was valid till April 2004.

4. It so happened that during these hard days the assessee was awarded work for Coal handling of Punjab State Electricity Board (PSEB) plant at Ropar. This was in the year 1986. It appears that some dispute arose in respect of the said contract and because of certain lapses/delays on the part of the assessee, the PSEB referred those disputes to the Arbitrator. The Arbitrator gave his award on 20th June, 1995 awarding a total sum of ₹ 2,29,57,583/- in favour of the PSEB and against the assessee. This amount was also to carry interest @ 12% per annum. This award came during two months of the sanctioning of scheme by BIFR as the BIFR had sanctioned the scheme on 01.05.1995. The PSEB got the aforesaid award filed in the in the court and

ultimately it was made rule of the court vide orders dated 10.10.2002 passed by the Civil Judge, Patiala. The assessee filed an appeal against this order which was also dismissed by the Punjab and Haryana High Court on 13th January 2003. No further appeal was preferred as a result of the decree became final.

5. Having regard to provisions of Section 22 of the Sick Industrial Companies Act (SICA), even when such a decree was passed, the PSEB was not in a position to get the decree executed. The assessee, however, treated the aforesaid decree passed in terms of award as liability accrued to it in its return filed for the Assessment Year 2003-04, corresponding to the financial year 2002-03, in which year the award was made rule of the Court. The Assessing Officer took a view viz. PSEB was not in a position to recover this amount without the consent/ approval of BIFR and, therefore, liability had not accrued. He rejected the contention of the assessee that since it was following mercantile system of accounting, liability to pay the aforesaid amount had accrued to it and Section 21 was only an embargo placed on the creditor not to enforce the said decree.

6. The assessee preferred the appeal against the order of the Assessing Officer. It was allowed by the CIT (A) vide order dated 23.01.2007. The department filed appeal against the order of the CIT (A) before the ITAT which was also dismissed vide orders dated 12.09.2008. However, on further appeal preferred by the department to this Court, orders dated 16.04.2010 were passed thereby remanding back the matter to ITAT on the question

whether the liability was a 'contingent liability' in view of the fact that prior permission of AAIFR/BIFR was required for the recovery of money, was obtained or not. The matter was heard afresh by the Tribunal which has culminated into orders dated 21.05.2010. By the impugned order the Tribunal has set aside the order of the CIT (A) thereby allowing the appeal of the Department and holding that the liability was contingent liability and therefore it had not accrued. It is in these circumstances that the assessee has approached this court by way of the present appeal preferred under Section 260A of the Act giving rise to the aforesaid substantial question of law.

7. Perusal of the impugned order of the Tribunal would reveal that the Tribunal has accepted the fact that once the award was made rule of the Court and decree was passed consequent thereto, the liability arose on 10.10.2002. It is also not in dispute that 10.10.2002 falls in the year in question. The Tribunal has also held that this aspect is rightly dealt with by the CIT(A) allowing the liability. In the opinion of the Tribunal the question, however, was as to whether such a liability was only a contingent liability in view of the declaration by BIFR that the assessee is a sick industrial company. On this aspect the Tribunal has come to the conclusion that it would indeed be a contingent liability in view of Section 22 of SICA which contains a non absentee clause and has overriding effect over the company law, any other law, memorandum and articles of association of the company or any other instrument having effect on the said Act or other law. Therefore,

Section 22 overrides the provision contained in Section 37(1) of the Income Tax Act as well under which the liability is claimed.

8. In order to appreciate as to whether the approach of the Tribunal in this regard is proper, it would be necessary to go through the provisions of Section 22 of the Act. It is a long provision and our purpose would be served by referring to relevant portion thereof which reads as under:

“22. *Suspension of legal proceedings, contracts, etc.*-(1) Where in respect of an industrial company, an inquiry under section 16 is pending or any scheme referred to under section 17 is under preparation or consideration or a sanctioned scheme is under implementation or where an appeal under section 25 relating to an industrial company is pending, then, notwithstanding anything contained in the Companies Act, 1956 (1 of 1956), or any other law or the memorandum and articles of association of the industrial company or any other instrument having effect under the said Act or other law, no proceedings for the winding up of the industrial company or for execution, distress or the like against any of the properties of the industrial company or for the appointment of a receiver in respect thereof [and no suit for the recovery of money or for the enforcement of any security against the industrial company or of any guarantee in respect of any loans or advance granted to be industrial company] shall lie or be proceeded with further, except with the consent of the Board or, as the case may be, the Appellate Authority.”

9. It would be seen that Section 22 deals with suspension of legal proceedings, contracts etc. Insofar as legal proceedings are concerned, it mandates that against such a company in respect of which inquiry under Section 16 is pending, or scheme under Section 17 is under preparation or consideration or sanction or the proceedings are in appeal i.e. before the AAIFR, no suit for recovery of money or for enforcement of claim against such company in respect of any loan or advance granted to the company shall lie or proceeded with except with the consent of the Board/AAIFR/BIFR, as the case may be. By the very nature of this provision, the only embargo put against the creditors is that the creditors are not entitled to file a suit or proceed with the suit and to enforce the claim. Whether this provision would make the liability a 'contingent liability' is the question. Answer is to be in negative.

10. As pointed out above, the assessee is maintaining mercantile system of accounting. It is also not in dispute and recognized by the Tribunal itself that once an award is passed and made rule of the Court, liability accrues. Therefore, under the normal circumstances it is but natural that liability had accrued against the assessee on 10.10.2002 when decree was passed in terms of the award. Only because the creditor is required to seek permission of the Board before proceeding to recover this amount would not make liability a contingent liability.

11. Answer is provided by a catena of judgments. First case on the point to which reference can be made is the judgment of this Court in **Bhai**

Sunder Dass & Sons Co.(P) Ltd. v. Commissioner of Income-Tax,
(2003) 259 ITR 33. It was a case where the assessee company had claimed deductions on the amounts in respect of commission payable by it to one Ms. Nellie Melson, a foreigner. It was also not in dispute that liability had accrued. However, before the payment could be remitted, permission of the RBI was necessary. On this ground the AO had held that for want of such permission, the occasion to make payment had not arisen and therefore the liability had not accrued. This view was upheld with the order of the Tribunal. Reversing the decision of the Tribunal and allowing the appeal of the assessee in that case, this court held that once it was found that the assessee was following mercantile system of accounting as per which any expenditure incurred by it was entitled to be deducted in the year in which the liability had accrued for the first time, mere fact that no amount could be remitted abroad without the approval of the RBI could be a reason to hold that liability had not accrued in the relevant assessment year. The following observations from the said judgment are worth noting:

We are unable to persuade ourselves to agree with the learned counsel for the revenue. It is common ground that the agreement under which the commission was sought to be paid did not require approval of the RBI. There was no restriction in entering into such agreement either. Thus, the accrual of liability to pay commission was not dependent on the RBI's permission to remit the sum abroad. The liability arises in terms of an independent agreement between the parties, which admittedly was not

governed by the provisions of FERA. In **CIT v. Shri Goverdhan Ltd.** [1968]69ITR675(SC) , the Apex Court had observed that "The legal position is that a liability depending upon a contingency is not a debt in presenti or in futuro till the contingency happens. But if it is a debt the fact that the amount has to be ascertained does not make it any the less a debt if the liability is certain and what remains is only a quantification of the amount : debitum in presenti, solvendum in futuro". As already noticed, in the present case, the restriction under section 9 of the FERA was only on the payment abroad, for which permission was required to be obtained from the RBI. Therefore, what was deferred was the discharge of the liability and not the accrual of the liability. At this stage, we may usefully refer to the observations of their Lordships of the Supreme Court in Coca Cola Export Corpn. v. **ITO** [1998-231-ITR-0200-SC) to the effect that the FERA contains stringent provisions for conservation of foreign exchange reserves of the country and for that purpose regulates certain payments and dealings in foreign exchange, etc., but the embargo placed in these provisions regarding remittances to be made abroad has nothing to do with the amount of disallowance under the Act.

16. In our opinion, Therefore, since the liability of the assessed to pay commission to the lady accrued under agreement dated 5-5-1970 and the assessed was maintaining its account on mercantile system of accounting, it was entitled to deduct such liability which had accrued during the period for which profits

and gains were being computed and, Therefore, the Tribunal was not right in law in restricting the deduction in respect of the commission to the amount actually remitted during the relevant year. Support to this view is lent by a decision of the Gujarat High Court in CIT v. **Super Scientific Clock Co.** [1999]238ITR731(Guj) , wherein rejecting the stand of the assessed that it was entitled to claim deduction on the basis of actual payment on receipt of the RBI's approval, it was held that under mercantile system of accounting liability accrues and is deductible in the year in which the same is payable and not in the year in which the assessed actually pays it and, further, the procedure for obtaining permission of the RBI to make payment does not postpone accrual of liability or make it contingent.

17. The decision of the Apex Court in **Nonsuch Tea Estate Ltd.'s** case (supra) does not advance the case of the revenue. As noticed above, in that case there was an absolute restriction against the appointment or re-appointment of a managing agent without the approval of the Central Government and, Therefore, till such approval had been obtained and granted, there was no question of any liability to pay the remuneration accruing, which is not the case here. Again, there was absolutely no restriction on the assessed entering into agreement with any person resident outside India for rendering of services. The restriction was only limited to the remittances of money abroad without the permission of the RBI.

12. Same view is taken by the Supreme Court in the case of **Coca Cola Export Corporation Etc. Vs. Income Tax Officer & Anr.**, 1998 (231) ITR 0200 SC.

13. At this stage, we would like to discuss the judgment of Gujarat High Court in the case of **CIT Vs. Super Scientific Clock Co.**, 1999 (238) ITR 0731 GUJ. In fact, this judgment is cited by the Tribunal in the impugned order to justify its opinion. However, a close and careful reading of the said judgment would suggest that the principle of law set out therein goes in favour of the assessee and against the revenue. That was a case where the assessee was to pay technical knowhow fee to a non-resident technical collaborator which became due under a contract in the year in question in which the said liability was claimed as business expenditure. The AO had, however, disallowed the same on the ground that the liability had not crystallized since no payment could be remitted without the approval of the RBI and under the provisions of Foreign Exchange Regulation Act (FERA). The Court held that the provisions of FERA had nothing to do with accrual of liability which arose in terms of the contract independent of FERA provisions – the fact that before actual payment is made permission of RBI is to be obtained does not make the enforceability of liability subject to it. This principle is explained in the following words:

5. We may usefully refer to ratio in case of Mrs. Chandnee Widya Vati Maddan vs. Dr. Col. Katial & Ors., AIR 1964 SC 978 which draws distinction between a contingent contract and a completed

contract in order to appreciate distinction between a contingent liability and the liability which is crystalised. It was a case in which parties had entered into agreement to sell certain property. The law required the vendor to seek necessary permission to such transfer. The suit for specific performance of such agreement was sought to be defended on the ground that the contract was contingent as its performance was dependent on permission to be granted by Collector. As to the obligation of the parties to the contract, the Court said :

"That the contract was not a contingent contract and that the parties had agreed to bind themselves by the terms of the document executed between them. The Court had got to enforce the terms of the contract and to enjoin upon the vendor to make the necessary application for permission."

6. In our opinion, the principle fully applies. Parties have entered into agreement on transfer of technical know-how with the permission of the Government of India. Under it liability of the assessee to pay fee for technical know-how accrued. The fact that actual payment could be made only with the permission of RBI, only put him under obligation to apply to the RBI for grant of necessary permission for releasing payment of amount to a non-resident. But its enforceability is not a contingent one.

14. Thus, reading of the judgment clearly demonstrates that it has taken same view as has been taken by this Court in ***Bhai Sunder Dass*** (supra).

15. We are, therefore, of the opinion that merely because proceedings could not be initiated by the PSEB against the assessee for enforcing the decree by way of execution for want of consent of the BIFR as required under Section 22 of SICA, it would not mean that the liability had not accrued when it is found that the assessee was following mercantile system of accounting.

16. We, thus, answer the question in favour of the assessee and against the Revenue. As a result this appeal is allowed holding that the assessee would be entitled to the deduction of the aforesaid amount on the basis that the liability had accrued in the year in question.

(A.K. SIKRI)
JUDGE

(M.L.MEHTA)
JUDGE

August 10, 2011
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